

## **The Social Consequences of Structural Adjustment Reforms in Tanzania**

**Stergomena L. TAX**

Graduate School of International Political Economy, University of Tsukuba, Ibaraki-ken 305-0006, Tsukuba City, Tennodai 2-1, Ichinoya 32-805, Japan. The author wishes to thank the founder of this Journal, Dr. Aziz Ponary Mlima for the initiative. She is also grateful to Dr. Gratian Bamwenda for his helpful suggestions and two anonymous referees. The author alone is, however, responsible for any errors or omissions.

**Abstract:** According to structural reform advocates, market-oriented strategies produce sustained economic growth. Experiences of some countries, however, have shown limitations of liberalization on big bang approach. In the mid-1980s, Tanzania plunged into an economic crisis. Responding to the crisis, the International Financial Institutions became very critical about Tanzania's development policies. In 1986, Tanzania entered into agreement with the IMF and embarked on a structural adjustment program. Although Tanzania is also hindered by the supply-side constraints that go with a lack of development, the structural adjustment measures have not paid attention to the long-term elasticities. Thus, the long-term has been sacrificed to the short-term. Exploring the social consequences of structural reforms in Tanzania, this paper concludes that, while the IMF imposed measures have been severe, they have recorded limited results.

### **Introduction**

The most predominant policy framework of the past two decades has been economic reforms under the structural adjustment programme, which has been imposed on Sub-Sahara Africa (SSA) by international financial institutions (IFIs). During the 1960, it was widely accepted that the major growth hindrance in Sub-Sahara Africa was capital shortage. Starting 1980.s, Tanzania like most of the SSA counties plunged into economic difficulties with balance of payments difficulties at the center. Responding to the economic stagnation, and the balance of payments difficulties, the IFIs (in particular the International Monetary Fund - IMF and The World Bank) and the Donors became very critical about Tanzania's development policies. The country's problem was no longer viewed as capital shortage but rather as of policy failure. Faced with a balance of payment crises, Tanzania could no longer borrow from the international finance market, the only alternative was to turn to the IFIs; the World Bank and the IMF, whereby assistance could only be granted on the condition that the country implement structural reforms<sup>1</sup>. "*We have to accept things that are not in our interest because there is no other way out*", *Pscoal Manuel Mocumbi, October 2000*.

In economic terms, a structural adjustments programme means a series of changes in number of key policy parameters<sup>2</sup>. Nonetheless, behind this 'technical' fascia that justifies policy changes by reference to 'economic rationality', 'efficiency' and fiscal prudence lies a number of unstated but contestable far-reaching social consequences<sup>3</sup>.

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<sup>1</sup> Under the Structural adjustments, loans and assistances are conditioned on the implementation of a series of conditions seeking to restore growth and stability by recasting relative prices, domestic expenditure and type and degree of government intervention in the economy.

<sup>2</sup> The policy parameters include liberalization of trade, devaluation of currency, dismantling price controls and subsidies, privatization, reducing government deficits and government spending, as well as eliminating other forms of protectionism.

<sup>3</sup> The discussion of the underlying theory of such policies is beyond the scope of this essay. The focus is on the consequences of such policies.

## Methodology and Hypotheses

This paper qualitatively and descriptively underscores the development challenges, describes the origins of the economic difficulties in Tanzania, and addresses the social consequences of adjustment reforms in the country. The paper hypothesizes that while the IFIs argue that the market-oriented, private sector led strategies are capable of generating sustained economic progress, the IFIs have not paid attention to the long-term elasticities. In doing so they have pressed measures that are more severe than necessary, while sacrificing the long-term to the short-term. The measures undertaken have promoted progressive inequalities, and widened poverty in the interest of immediate growth, while the agriculture export drive has resulted into falling prices and subsequently into economic losses for the majority. It is further hypothesized that, whereas the liberalization of the foreign exchange market might improve capacity utilization, especially in the manufacturing sector, through easier access to imported inputs, the overall marginal capacity utilization might be marginalized due to the inadequate demand which domestic firms might face under a liberalized regime. The rapid exposure of domestic industries to the international competition might affect the manufacturing sector negatively.

### Background and Basic Features of the Tanzanian Economy

One of the difficult development challenges of Tanzania like most of other Sub-Saharan Africa (SSA) is how can she graduate from sluggish to self-sustaining growth. To attain a self-sustaining growth, a number of requisites are indispensable. To the contrary, such requisites are non-existent in Tanzania. The challenge of social and economic betterment predominantly persists. Tanzania is an agrarian developing country consisting of a large traditional rural agriculture sector and a small urban based commercial sector. The majority of its population is engaged in subsistence activities. Agriculture accounts for 50-60% of the gross domestic product (GDP), and about two thirds of exports. Thus, the prices of agricultural products in the world market play a significant role in economic development. The employed labor force, that is to say those who are in the some way connected with the market, is small, comprising only about 10% of the population. Industrialization is remote; the share of manufacturing and industry production in the total GDP has declined from 20% in the early 1970s to about 14% in the early 1990s<sup>4</sup>.

The colonial rule concentrated on the development of cash/export crop production as well as on the building-up of the infrastructure for the colonial 'export enclave'<sup>5</sup>. The indigenous people were discouraged to engage in export crop production, but rather encouraged to supply their labor to the plantations. Consequently, the spread of the modern economy into the traditional economy became limited. At independence in 1961, the economy was at a very early stage of development, with limited human and physical infrastructure, less stable infrastructures, less settled administrative institutions, and weak private institutions with limited capacity.

The inherited economy was a dependent economy, whose structure relied heavily on the production and export of a few primary products to European Markets<sup>6</sup>. Apart from the diamond mining, a large part of the export sector was made up of either un-processed or semi-processed products<sup>7</sup>. Industrial activities were at a very low and rudimentary level. Secondary activities, which included

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<sup>4</sup> Statistics are drawn from United Republic of Tanzania: Budget speech, and form economic surveys, 1984-1994.

<sup>5</sup> Basic infrastructure like transportation, forward and backward linkages, marketing, storage facilities and credit facilities were only to facilitate the colonial plantation's production and export to European markets.

<sup>6</sup> Pratt (1976), discusses in details the structure of production in Tanzania during the early period of independence.

<sup>7</sup> Over 60% of the GDP was composed of primary products such as coffee, cotton, tea, sisal and cashew nuts.

manufacturing, processing and construction, formed about 13%<sup>8</sup>. The rest was tertiary activities. Communication systems linked a few towns to Europe and not to areas within the country. The only developed sectors equipped with infrastructure were enclaves of mineral, export crop plantation and production. The proportions of literate and educated people, was small, while the average life expectancy was low. For example, in 1965 only 40% of those with age to attend school had access to primary education. Not to mention college graduates, who were extremely few<sup>9</sup>.

### **Perpetuation of Colonial Legacy Through Foreign Aid**

Although Tanzanian farmers were obligated to grow cash crops for European industries by the colonial rule, the agriculture infrastructure, like technology, finance, transport, marketing, storage facilities and agricultural implements was poor. The Facilities in place did not cater for the requirements of the small-scale farmers, who consisted the majority but rather in accordance with the colonial requirements, i.e., to facilitate production and transportation of minerals and crops to the Europe. Although some goods (particularly the perishables) needed proper storage, and comparative opportunities existed within the country as well as in the neighboring countries, the required infrastructure, trade, marketing and other facilities were not adequately established<sup>10</sup>. At the same time irrigation was on small scale<sup>11</sup>.

Few years after independence i.e., in 1967, Tanzania adopted the policy of *Ujamaa* and Self-reliance with the objective of enhancing equity and welfare of the majority, correspondingly, emphasis was attached to the improvement of the agriculture sector. However the country was poor, with inadequate and weak structures. To confront the task of improving not only the agriculture sector, but also the overall economy, the country had to rely on foreign resources. The country was able to mobilize external finance, the assistances, however, were not free of conditionalities to suite donors' interests<sup>12</sup>. Conditionalities such as tying aid to procurement allocated aid to the areas of donors' preferences and in a way that perpetuated the colonial settings, while improving the level of productive forces within the existing ownership structures.

Whereas, improved welfare and standard of living for the majority required improvements in the agriculture sector, particularly small scale farming, which not only employs the majority but also comprises a large share of exports earning, aid inflows to the sector were not directed to the basic requirements that could have enhanced the sector's performance. Aid inflows toward irrigation, technological improvements, credits, education, storage, transportation, and marketing which are the basic needs were very limited. Instead, aid was used to put in place semi-processing industries, roads and railways (e.g., the Tazara Railway)<sup>13</sup>, which were to ensure a continued smooth transportation of

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<sup>8</sup> Data drawn from URT; "Twenty Years of Independence, A Review of Political Economy", 1986.

<sup>9</sup> Ibid.

<sup>10</sup> Transportation cost have been intrinsically high, Collier et al. (1999).

<sup>11</sup> About one third of the available land in Tanzania is too dry for rainfed agriculture, Wood (1998). Since the 1970s there has been a trend of deterioration in rainfall.

<sup>12</sup> Taking transport infrastructure as an example, its importance cannot be overstated. Tanzania is a relatively large country with sparse population. Therefore, the efficient movement of food between regions, movement of production inputs to production sites and output to markets requires efficient transportation. Apart from its direct contribution to GDP the sector is the second in facilitating the activities of others sectors, in 1980s it ranked second highest in terms of forward linkages, (Bank of Tanzania operation reports and Economic Surveys). The improvement of transport infrastructure reduces costs, enlarges the size of the market and thus, renders positive effects on both supply and demand conditions. Although the government in its second five-year development plan adopted a policy of an all-weather low cost road system and the expansion of the road capacity to cover wide area, the plan could not be materialized. The government was severely financially constrained, while donor preferred to channel their assistances elsewhere.

<sup>13</sup> TAZARA was the only new railway, which was constructed. The construction of TAZARA was put in place so as to open up

cash crops and mineral to external markets. Donors appeared to have devoted little efforts in designing forms of aid and defining areas in which the impact of aid could have been truly valuable.

On the other hand, the cash crops (raw and semi-processed) acquired very low prices in the world market; however, the finished goods, which were brought back as processed goods/finishes goods, were exorbitantly priced. It is also important to note that under the basic industry strategy (BIS) that was adopted in the 1974 a significant portion of aid was channeled import dependent investments. Although the sustenance of these import dependent investments required the availability of foreign exchange, adequate foreign exchange could not be generated domestically.

## **Background of Structural Adjustment Programme in Tanzania**

Since independence Tanzania has undergone a process of profound social economic changes. Immediately after independence, the country pursued a market oriented development strategy. In 1967, the country adopted the Arusha Declaration policy that gave a dominant role to the state with the intention of speeding up the development process. The Arusha Declaration emphasized the provision of social services and better living conditions for the Tanzanian people. In mid 1970s, Tanzania sought industrialization as an antidote to the inherited colonial economic structure. The policy emphasis shifted from the agriculture to the manufacturing sector. In 1974, Tanzania adopted the basic industry strategy (BIS) that emphasized import substitution and simultaneous expansion of heavy producer and consumer goods industries. The industrialization policy, however, led to a good lead of capital-intensive investments that were import dependent. On the other hand, the manufactured goods were rarely competitive internationally.

The early post-independence years showed a relatively fast economic growth, later it however slowed down, and in some years the GDP growth rate was even negative. The reliance on exports of primary products, made Tanzania face highly unstable markets and particularly vulnerable to the unfavorable terms of trade and other conditions in international markets. In mid 1970s, the prices of most of the primary products fell and international terms of trade worsened. The sharp deterioration in the terms of trade, the historic high during the 1980s deepened the country's economic difficulties<sup>14</sup>.

As the country faced a situation of declining export earnings and budgetary revenues, the government employment and expenditure had expanded. With her merge foreign exchange earnings from exports of the few primary products, and receipts from foreign aid, the country had to import almost all of her capital goods, intermediate inputs requirements, some consumer durables, and some food. As the deficits both in the trade balance and public finance became unsustainable, the country had to compress imports. The import compression resulted into a depression of investments, production and consequently into a further decline in exports earnings. In addition to the above, other external factors aggravated the situation<sup>15</sup>.

Following the foreign exchange crisis the Tanzania economy was virtually brought to a stand still. On one hand, agricultural exports declined as a result of both a decline in export prices and a decline in

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the south for the exploitation of the mineral resources, and to provide Zambia (a neighboring country) with an outlet.

<sup>14</sup> Deterioration in the terms of trade has been estimated to account for a reduction in African growth rate relative to that of other developing countries by 0.7 percentage points, Ndulu, (1996).

<sup>15</sup> The two successive oil shocks of 1973/74 and 1978/79 forced Tanzania to use increased share of foreign exchange receipts on oil imports. The break-up of the East African Community in 1977 as well had a detrimental effect on the economic infrastructure and communications. The war with Uganda in 1978 brought disruption in agricultural production and transport services, and a sharp rise in imports of military hardware and equipments.

production. On the other hand, the BIS had created a manufacturing sector, which while contributing marginally to the economy, was a heavy net user of foreign exchange. Although there was a build up of high import demand, Tanzania was forced to reduce the value of imports by 37% in three years; from US\$ 1384 million in 1980 to 870 million in 1983<sup>16</sup>. As a consequence of shortage of foreign exchange to import the required intermediate goods<sup>17</sup>, the capacity utilization in the industrial sector declined to below 30%<sup>18</sup>.

The government also faced increased payment arrears. Prior to the 1980s crisis, the country had reached a Stand-by-Arrangement with the IMF of SDR 179 million for a period of up to May 1982. Tanzania faced difficulties in meeting the conditionality and the performance criteria<sup>19</sup>; subsequently the IMF drawings were suspended after the first tranche that was released in late 1980s. The loss of foreign exchange, which resulted from the suspension, was partly compensated by commercial borrowing (supplier's credit) that amounted to US\$ 165 million over the years 1980-83. These credits contributed strongly to an increase in payment arrears from US\$ 302 million in 1981 to 445 million, and exceeded the total export earning by 30% in 1983<sup>20</sup>. Notwithstanding the economic difficulties, bilateral donors withheld their aid inflows. The total grant to Tanzania net of technical cooperation was reduced by 45%, from US\$ 485 million in 1980 to 265 million in 1985. Total aid including net concessional loans (net of technical cooperation grants) was reduced by 30% from US\$ 492 million to 345.5 million in the same period<sup>21</sup>. These developments affected all sectors of the economy. Agriculture and manufacturing sectors suffered severely from the failure to acquire the necessary inputs.

The intensity of the economic crisis, the inability of the national efforts to revive the economy<sup>22</sup>, and the pressure from the donor community under IMF/World Bank forced Tanzania into an agreement with the International Monetary Fund (IMF) and The World Bank on a structural adjustment program. In 1986, Tanzania agreed to pursue an Economic Recovery Programme (ERP). The ERP may be interpreted not only as an attempt to solve the economic crisis, but also an attempt by the government to accommodate the demands of the IFIs in order to overcome the foreign exchange constraint<sup>23</sup>.

While, the ERP emphasized that the imbalances in the economy leading to crisis were due to poor policies<sup>24</sup>, there are doubts, however, if the proposed and adopted measures really address these problems, and imply fundamental changes for the betterment for the Tanzanian economy. The reforms appear have ignored some sectors of the economy where reforms seem most urgent, and have not dealt with the underlying economic hindrances. The country is yet to attain structural transformation and remains with narrow, rigid and vulnerable productive bases. The country has not been able to attract private foreign investors, but has remained heavily dependent on foreign aid.

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<sup>16</sup> Bank of Tanzania; Operations reports, 1982-94, and Budget speeches by the Ministry of Finance (1986-95).

<sup>17</sup> Export earnings fell from US\$ 614 million in 1981 to 384 million in 1983 i.e. by 38% within two years, (data from Operations Reports by the Bank of Tanzania (1982-1994).

<sup>18</sup> Ibid.

<sup>19</sup> Especially on the devaluation, budget restraint, credit restraint, and elimination of subsidies.

<sup>20</sup> Bank of Tanzania report (1986).

<sup>21</sup> Data are extracted from the Report on "Aid effectiveness in Tanzania", by the Ministry of Finance (1995).

<sup>22</sup> Responding to the crisis, Tanzania tried to formulate and implement a national programme, the national economic survival programme (NESP) in 1981-82, the programme, however, did not achieve the intended goals.

<sup>23</sup> Such a step seemed necessary so as to attain increased foreign inflows from both the World Bank and bilateral Donors (who tied their support to the recovery program).

<sup>24</sup> Among others, it emphasizes the "insufficient resources for agriculture development as compared with the high priority given to industry, "inadequate producer incentives and marketing/distribution systems in agriculture, "expansionary fiscal and monetary policies" and "the rapid growth in the government sector".

## Social Consequences of Adjustments Policies

For sustainable economic growth, a country requires both physical and human capital. Human resources development ensures effective and efficient utilization of capital. Human resources development is the process of increasing the knowledge, skills, and the capacity of people. Additional ways for human resources development are improvements in health of the people, the improvement of nutrition, and thus the overall quality of life. Such improvements increase the working capacity and productivity, i.e., on man-hour basis and over a working life. Both improvements in health and nutrition are related, and like education contribute to economic growth Schultz (1989). Education is one of the human resources whose distribution affects households' income, and thus standard of living. Education assists in reducing poverty and improving health, and it promotes the only asset poor possess, labour, Isakson (1999).

Under the Arusha declaration, efforts to improve education and health services were put high on the agenda. The social sector received substantial amount of resources, both from foreign aid as well as from the government. Following the structural reforms not only the government allocations to sector declined, but there was also a shift in aid strategy towards programme support, (mostly balance of payment and commodity support). Consequently resources to the sector declined considerably. In the 1970s the government allocation to education was 20% and 13% to health as compared to 7% and 6%, respectively in the beginning of 1990s<sup>25</sup>. On the other hand, foreign aid disbursement to the social sector fell to about 20% in the 1980s, from about 85% in the early years of independence and fell further to about 19% in the early 1990s, appendix 1 depicts the movements. The social sector has also been negatively affected by the cost sharing system, which was introduced following the reforms<sup>26</sup>. While the reforms have resulted into deterioration of income and standard of living of the majority (as it is explained further in the text), people are required to pay user fees.

The social indicators in Table 1 suggest that while in the 1970s, Tanzania had a development, which in several respects was better than the average for SSA, the situation turned around. During the 1970s Tanzania managed to achieve a very respectable enrollment rate and literacy levels as well as reduced mortality rates. However, as a consequence structural reforms, the early improvements were eroded. Many schools have fallen into decay, schools lack books and other supplies, teachers are often inadequate and sometimes unskilled, the school buildings have deteriorated. Evaluation on high education also shows that as a result of shortages of qualified teaching staffs and teaching equipment the quality of education has deteriorated. Ability to improve the situation is questionable; let alone initiating any new education projects that might be desirable.

Table 1: Selected social indicators for Tanzania and SSA, 1970 to 1994

Indicator	1970-1980		1985-1990		1990-1994	
	Tanzania	SSA	Tanzania	SSA	Tanzania	SSA
Life expectancy at birth (years)	47	47	48	49	48	51
Infant mortality rate	122	127	117	118	115	107
Average daily calorie intake	2244	2107	2229	2040	2206	2120
Primary school gross enrolment rate (%)	93	70	72	68	63	69

Source: The National Accounts, and Bureau of Statistics, 1986-1996 publications.

<sup>25</sup> Data is from URT: "Conference on aid effectiveness in Tanzania", by The Planning Commission, (1995).

<sup>26</sup> Under the systems of cost sharing people are required to pay user fees for social services like health care, water provision and education.

Table 1 further indicates that, while Tanzania does well with regard to caloric intake, the achievements of the 1970s on the remaining three indicators have deteriorated. Life expectancy had hardly increased, the infant mortality has decreased more slowly than in SSA. The most dramatic changes, however is the large decline in primary school enrolment, from 93% during 1970-1980 period way above the average of SSA, to 63% in the 1990-93 period. The provision of water supply has also been deteriorating. In the early 1980s about 60% of population had access to water. In the early 1990s almost half of the system were out of order due to breakdown, incapacity of operations and lack of maintenance. Coverage is very low, only about 28% of the population<sup>27</sup>. All these indicate a serious decline in the social sector. Inequality and poverty have also increased. The Gin-coefficient was estimated at 0.44 in 1976/77 it rose to 0.57 in 1971 (World Bank, (1993)). As a consequence of poverty people (the majority of Tanzanians) are incapable of accessing education and health services, maintain or manage the facilities that provide social services on the basis of user fees.

The above-explained direct social consequences are not the only consequences of structural reforms. Linking the adjustment reforms with distributional impacts, it is observed that the majority of Tanzanian who are farmers and workers have suffered dramatic declines in living standards. The underlying focus of the reforms on export orientation has neglected the food sector. In cases where there have been improvements in food output, the improvements have been generally by accident of nature and not by the design of policy reform. Food policy have tended to be confined largely to removal of subsidies. Whereas food subsidies were financed out of the recurrent budget of the government, its removal did not raise producer prices, but instead reduced the budget deficit, Campbell (1990). The reforms are designed to shift the terms of trade in favour of export crops, while nothing is done to remove the non-price constraints on expanding food production. In the final analysis, these weaknesses are reflected in spirals of inflation caused by food output lagging behind demand. As food prices rise and reduce the competitiveness of exports, the government is pressed to devalue in order to restore the differential. Yet again, the consumer price index responds to food shortage and the cycle repeats itself.

The consequences of adjustments policy and the emphasis on export drive are beyond that of supply of food. World Bank argues that liberalization and privatization of marketing will result in a more efficient marketing system; retaining smaller marketing margins and thus passing on to the producers a larger share of final prices. Combined with devaluation of the Tanzania Shilling (TShs.), this should give producers of export crops a strong incentive to increase their output, with the result that Tanzania should increase its agricultural exports and hence exploit better its comparative advantage in international trade.

So far, there is no sign that such a process is taking place. Table 2 indicates that the exports volume of Tanzania's major exports has not been at a higher level in 1991-94 than in the crisis period 1982-85, in spite of the real devaluation of more than 80%. On the other hand, due to a dramatic price decline of 33% between 1987 and 1994 (mainly caused by coffee), the exports value in US\$ terms of these crops was 28% lower in 1994 than in the crisis period 1984-85<sup>28</sup>. Tanzania accounts for only small shares of total world exports of the commodities. In that case, the prices Tanzania acquires on the world market are not affected by changes in its own volume of exports, the price and income elasticity of these commodities are very low. The widespread adoption of the IMF and World Bank programmes has led to an expansion of world supply and a corresponding decline in the world prices. As an advice from IMF and The World Bank, and as aid conditionality several countries competing with Tanzania on the world market have tried to ease their balance of payment crises through export

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<sup>27</sup> Data is drawn from the economic Survey, Planning Commission, 1993.

<sup>28</sup> Data is drawn from trade and statistics reports, Bureau of Statistics, 1990 –1996.

drive. That was the main reason for example of the collapse of the International Coffee Organization in 1989, and the subsequent dramatic decline of world prices of coffee, Tanzania's major export crop. The average export price of Tanzania coffee dropped by 27% within one year from US\$ 2164 per tone in 1990 to US\$ 1370 in 1991. Prices for tea and cashew nuts have also declined considerably<sup>29</sup>.

Table 2: The exports volume of Tanzania's major exports, 1982 to 1994

Year	Real exchange rate US\$/TShs <sup>1</sup>	Indices of real exchange rate 1985=100	Six Major exports crops <sup>2</sup>				Value of manufacturing Exports as % of total Merchandise exports
			Export volume indices 1985=100	Export unit value indices US\$ 1984=100	Export value indices US\$ 1985=100	Export value as % of total Merchandise exports	
1982	0.1742	98.8	136.0	92.9	126.3	61.2	10.0
1983	0.1862	105.6	112.1	83.8	93.9	60.6	9.1
1984	0.1873	106.2	102.8	88.9	91.4	64.5	11.6
1985	0.1764	100.0	100.0	100.0	100.0	69.0	8.5
1986	0.1988	112.7	83.4	87.8	73.2	68.4	11.4
1987	0.1376	78.0	92.5	105.5	97.6	75.3	11.2
1988	0.0883	50.1	99.6	75.4	75.1	57.9	18.3
1989	0.0727	41.2	103.1	81.2	83.7	60.3	19.4
1990	0.0607	34.4	100.7	78.8	79.4	56.0	24.1
1992	0.0510	28.9	112.5	66.3	74.6	50.1	26.0
1994	0.0445	25.2	102.7	80.0	71.9	58.4	18.5

Source: Bagwacha 1993, and Tanzania Economic Trends Vol. 6 Nos. 1-2, July 1993.

<sup>1</sup> Nominal Official exchange rate divided by the weighted consumer price index for industrial (OECD) Countries and multiplied by the consumer price index for Tanzania.

<sup>2</sup> Coffee, cotton, sisal, tea, tobacco and cashew nuts, accounting for an average of 62% of the value of Tanzania merchandises exports in the period of 1982-1992.

“The World Bank's recipe of agriculture export drive as a component of structural adjustment in countries such as Tanzania suffers form a serious fallacy of composition. Because price elasticity as well as income elasticity of the primary commodity are typically low, an overall export drive and/or struggle for world market shares by several countries at the same time lead invariably to price collapses and correspondingly economic losses for the majority of countries in question”, URT (1997). From the preceding it is apparent that, consequences of adjustments policies on both food and cash crops production and earnings, have led the majority of Tanzanian to suffer dramatic declines in incomes and overall living standards.

A combination of an emphasis on the export drive with a clear ideological prejudice on the part of the IMF and the World Bank in favour reliance on market mechanisms and promotion of the private sector has other implications on the performance and structure of the economy. The adjustment programs were designed to improve foreign exchange allocation through emphasizing and stressing the need to ensure that the enterprises with access to foreign exchange are efficient in both economic and financial terms. Stated more directly, the emphasis was on better performance by moving towards a more transparent and open to all foreign exchange allocation system, so that the more efficient users of foreign exchange may gradually out-compete the less efficient users, Edwards (1989).

<sup>29</sup> Data is from Bank of Tanzania Economic and operation report, 1993.

Table 3: Average rates of capacity utilization in selected industries

Period	1970-1975	1976-1980	1981-1985	1986-1990	1991-1994
Rate of capacity utilization	61.9	60.2	51.6	51.8	49.5

Source: Computed from the National accounts, 1986 -1996 publications.

Note: This sample consists of relatively large, efficient parastatals viewed as critical by the then import licensing authorities. Typically capacity utilization is drastically low during the late 1970s and early 1980s.

Although, in general terms the above criteria for foreign exchange allocation are indisputable, the policy measures adopted in Tanzania have not been entirely complementary. From the supply side, in so far as availability of input is concerned, freer access to foreign exchange is likely to help firm to meet their essential imported input requirements and thus improve the capacity utilization. Table 3 shows that the liberalization of foreign exchange has not enabled the manufacturing sector to improve capacity utilization. Nevertheless, it is somewhat simplistic in terms of economic logic to expect that liberalization of foreign exchange allocation alone would increase substantially capacity utilization. Liberalization of foreign exchange allocation emphasizes only the supply side constrains, i.e. of imports of essential raw materials. Firms are also faced with other several difficulties<sup>30</sup>. Although import liberalization eases some supply side constraints, it also exposes the firm to foreign exchange competition and usually reduces the size of its market. Malfunctioning of economic and social infrastructure is perhaps even a more serious problem. Additionally, in a backward economy like Tanzania, despite the availability of the required imported raw materials, in the short run, negative demand may become the binding constraint for many firms.

Using the change in market share we evaluate the effects of import liberalization on demand, while examining the effects of exposing domestic firms to competition. In doing so, as shown in Table 4, we find that the market share of domestic manufacturing industry has decreased quite drastically following the liberalization of imports. Moreover, the manufacturing value added in the liberalization period 1986-1994 was considerably low as compared to 1974-79, and even lower than during the crisis period 1980-85. This indicates a “Demand-squeeze” since the fall in market share is not accompanied by dramatic decline of total market size in 1986-1994 as compared to the preceding period.

Table 4: Market share of domestic manufacturing industry 1970-1994

Period	Market share* in %	Indices of manufacturing value added at constant 1976 (1970-73 = 100)
1970-1973	61	100
1974-1979	67	128
1980-1985	72	113
1986-1994	36	109

Source: Computed from the National accounts, and Trade and statistics reports, Bureau of Statistics 1986-1995.

\*Market share is calculated as the ratio of the manufacturing sector/value added to value added plus Imports of consumer goods.

While the demand conditions faced by domestic manufacturing firms deteriorated sharply since import liberalization, and at a rapid pace, the advocates of structural reforms are optimistic that the exposure of domestic firm to foreign competition will force most of them to improve efficiency for survival over time. This schumpeterian argument of ‘creative destruction’ in a market economy may

<sup>30</sup> In his study of factors behind differences in per capita growth rate across Africa, Svendsen (1995), shows that a firm is faced by a diametrically opposite problems from both the supply and the demand side.

turn out to be over-simplistic in a country like Tanzania. With the very poor economic and social infrastructure even relatively efficient domestic firms are at a great disadvantage to compete in an open economy. Until these structural facilities are brought at least to a minimal functioning level, the microeconomic preconditions for the working of a competitive market mechanism for 'creative destruction' cannot be expected.

Although the use of price incentives created through devaluation is expected to stimulate manufactured exports and hence diversification of export, a sudden and premature exposure of domestic manufacturing firms to international competition may also cause industrial stagnation or even, in the worst case, trigger off a process of de-industrialization. And, indeed there are some early signs of such adverse developments in Tanzania. As shown in Table 4, the market share of domestic manufacturing industry fell from 72% in 1980-85 to 36% in 1986-94, while value added fell from an index of 128 in 1974-79 to 113 in the crisis years 1980-85 and further to 109 in 1986-94<sup>31</sup>. Moreover, the share of manufacturing industry in total GDP at current prices continued to fall, from 7.4% in 1987 to a historical low of 3.6 percent in 1994.

In 1990 and 1991, the value of manufacturing exports as a share of the total value of merchandise exports rose above previous levels, to 24.1% and 26% respectively. However, this increase was to a large extent due to a decline of export value of traditional crops. There was a decline of 11% from 1989 to 1991 following the dramatic fall in prices, especially of coffee. In 1992 the share of manufacturing exports in total export value declined again to the level of 1988, and the value of manufacturing exports in 1992 was only US\$ 60.9 million as compared to 63 million in 1988<sup>32</sup>. Additionally, the produced goods faced a weak demand in the stagnating economy.

## Summary and Conclusions

The results of the analysis presented in this paper are in line with the hypothesis that the reforms have resulted into deterioration of income, standard of living of the majority, and thus intensified poverty. In contrast to the hypothesis that the liberalization of the foreign exchange market is expected to improve capacity utilization through easier access to imported inputs, it has been observed that capital utilization has not increased significantly, while domestic goods have faced contracting demand. The present evidence points more to the "destructive" effects of foreign competition than to the "creative" effects on domestic industries in Tanzania.

Tanzania's development difficulties are persistent. The country faces a limited capacity to adjust quickly, while possibilities for rapid economic restructuring are few. Tanzania is hampered by the supply constraints that go with a lack of development (structural problems). Overcoming structural difficulties require long-term investments. Yet these long-term investment processes are frequently interrupted by short-term crises caused by external shocks, and weather-induced crop failures. Tanzanian principal commodities are commodities with limited prospects in current circumstances. Neither households nor firms have as yet sufficiently created the social institutions to promote growth<sup>33</sup>. It is, however, unfortunate that the adjustment reforms have not been sensitive to the

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<sup>31</sup> Computed from the National accounts, Bank of Tanzania, Trade and statistics reports, Bureau of Statistics and the Economic and Survey by the Planning Commission of Tanzania, 1986-1996.

<sup>32</sup> See Table 4 and Ministry of Finance: Budget speeches for 1993/94, Dar es Salaam 1993.

<sup>33</sup> Exports depend on a small number of primary commodities that are vulnerable to unfavorable weather conditions, and terms of trade. At the same time the manufacturing sector is small, infrastructures are poor and the country lacks a prominent private sector.

situation in Tanzania. The social-economic structure and other important factors in the economy have been left aside; as if they do not carry any weight. The relationships between the short-term adjustment programme, designed to stabilize the balance of payments and the requirements of medium and long-term development have not been taken into considerations. There is no much point in improving price signals if firms capable of responding in a competitive framework cannot receive the signals.

In view of the foregoing findings, it recommended that the improvement of the productivity of the manufacturing sector be carried simultaneously with the improvement of the agriculture sector. The agriculture sector will have to produce the surplus from which industrialization will have to be financed, just as it did everywhere else in the world. The creation of the agricultural supporting infrastructures should focus on streamlining the required facilities, ancillary services and linkages in a direction that will ensure a healthy growth of both markets, i.e. the domestic market as well as for exports, while taking into consideration the welfare of the majority.

The separation between the use of price mechanism for efficiency purpose and ideological preference of free market is as well indispensable. Development in countries like Tanzania requires both the private and public sectors. The pendulum must not swing so far towards the private sector that the desirable functions of the public sector are neglected. For private activity to become more prominent of its accord, the government should provide the conditions in which private activity can flourish. Firms in Tanzania operate in a very unfavorable macro-environment. The poor social and economic infrastructure makes Tanzanian firms severely handicapped to face international competition and to create new investments. In view of their late start, it cannot be expected that they by themselves can develop the technological innovations and other competitive assets to survive and even grow in a highly competitive (world) market without government assistance<sup>34</sup>. The doctrine of competition need not be interpreted in a narrow way to mean exclusively competition within the sphere of private economic activity.

While a more open orientation for an economy is desirable, the timing and sequencing of opening up must relate with care to the country's export capacity, the state of the world market, the ability of domestic producers to benefit from foreign competition as well as the social effect and subsequent economical effects resulting from the undertaken measure. The pace of the adjustment reforms must be sensitive to the country's capacity to adjust and to benefit from opening up the economy to international market forces. The pace should be carefully synchronized with an effective national policy, while taking protection against swings in foreign currency earnings and paying great attention to supply as opposed to demand issues. It is also important that adjustment measures be harmonized with actions to promote all necessary aspects of change. When better price incentives are set for domestic producers, attention must be paid to ensure that the non-price elements of improved production are also in place.

Emergency situations should be met from contingency funds so that essential investments can

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<sup>34</sup> It is only in the United Kingdom and the United States of America could the market develop the private sector and thus the industrial sector at the early stage of development, which is why they are still champions of free market. But no other nation could industrialize without a conscious industrial policy and some protection, not even the Asian Tigers. Even when the private sector plays a greater role in investments, the government will be required to undertake certain public investments (supportive infrastructure). The aim should be to acquire the capability to perform those activities in which local capability to carry them out is limited or needs to be strengthened. The government should assist in the creation and promotion of competitive firms, commercial networks, markets, institutions, infrastructures, legal and regulatory framework, ancillary services, which are weak or non-existent. Direct assistance to the private sector activities among others should give emphasis to access to technologies.

continue without interruptions. The short-term and long-term adjustments programme should be harmonized. Although the IMF and the World Bank collaborate on trade liberalization, and price reforms, the non-price elements are however, largely left to the World Bank and the government. Exchange over such matters could be instrumental in producing greater realism about the time-path of successful adjustments. There is a need of improved collaboration between the World Bank and the IMF, so as to achieve two main purposes. First, a better relationship between policy instruments and actions and secondly, a greater harmony between short-term adjustments and longer-term development.

While International institutions and donors are putting increasing pressure on governments to make use of market forces, they are the ones who are distorting the competitive process through 'asymmetrical liberalism'. For example, the goods Europe imports from Africa free of duty are the agricultural products it cannot produce. Imports of processed products are mostly subjected to high duties, Elliesen (1999). There is no good match, for example, between trade policies urged on recipients by IFIs and other donors and their own trade policies, which greatly harm poor countries. The alternatives should be scrutinized thoroughly, and all practices that create unhealthy competition should be brought to an end.

Additionally, a due regard should be paid to the distributional effects. That is to say, adjustments to the general world economic conditions must not be made at the cost of poor people. The countries social-economical problems, and the corresponding social inequalities and vulnerability to crises of different social groups need to be considered. Poverty is not an individual problem, but a social one. Poverty can be alleviated where there is a stable social community. International Institutions must therefore, support the societies in finding a middle course between preserving social structures and broadening individual opportunities. Society's distribution of wealth is crucial in poverty alleviation, however it is important to note that, it is not only about monetary distribution, but also equipping the poor with the means of production. In the case of Tanzania these will include access to education, health, credits, irrigation, storage, transportation and marketing facilities<sup>35</sup>.

It is equally important that the reform policies to be discussed and agreed upon by both parties and be implemented based on the priority needs of the recipient. Structural reforms have been characterized by much asymmetry (both parties do not negotiate on an equal footing). IFIs have claimed to have "good intentions", but it should be realized how different the effect of "good intentions" might be. Tanzania has been inclined to accommodate the IMF/World Bank's position. This inclination is sustained by the perception that disagreement with IMF/World Bank would induce the withdrawal of support not only by these Breton Wood Institutions, but also by the other donors. In this regard, the Tanzanian capacity to negotiate and undertake policy analysis should also be strengthened. Importance should be attached to the capacity to engage in dialogue, and to examine policy alternatives. Policy proposals and drafts for negotiations should originate from the government. The most important starting point is to ensure that the Policy Framework Paper (PFP); the basis for negotiations with the IFIs and the other donors is prepared by government. It is also indispensable for donors to strengthen their capacities to understand the institutional, economic, political and social influences in Tanzania, an understanding that lags far behind economic and technical competence of the IFIs.

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<sup>35</sup> The IFIs are putting much pressure on the government to privatize and introduce cost sharing systems on social services, whereas in most of the developed nations education is highly subsidized if not provided free of charge, and there are well established health insurance systems. Taking Europe and Japan as an example, every one has the right and the access to elementary through high school education free of charge.

Summing up, firms in Tanzania are not simply inefficient in terms of internal organization, but they also operate in a highly unfavorable macro-environment, with very poor economic and social infrastructure. Until such structural facilities are brought at least to a minimal functioning level, and an efficient maintenance of economic and social infrastructure is put in place the microeconomic preconditions for the working of a competitive market mechanism for creative destruction may just be over-simplistic and cannot be expected. The outward oriented economic strategy cannot contribute to economic growth in vacuum. A link between a liberal regime and economic success must be in place. Within this trust, adjustment measures and economic policies should aim at putting in place a clear strategy that can promote growth and balance of payments stability, while taking into consideration the welfare of the majority.

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#### Appendix 1. Sectoral disbursement of foreign aid over time

Year	Social Sector	Economic Sector	Production Sector	Administration Sector	Multi sector
1965-66	85	0	15	0	0
1967-68	85	0	4	11	0
1969-70	53	28	14	4	1
1971-72	57	19	20	3	1
1973-74	40	14	31	11	3
1975-76	49	3	19	4	24
1977-78	38	6	20	23	12
1979-80	25	9	30	7	28
1981-82	21	1	28	3	46
1983-84	19	3	30	6	42
1985-86	19	8	28	8	38
1987-88	19	9	22	8	42
1989-90	19	6	27	3	45
1991-92	20	13	21	5	41
1993-94	17	32	13	7	30

Source: URT, “Conference on the effectiveness of foreign aid in Tanzania”, by the Planning commission, 1997.