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FISCAL AND MONETARY BURDEN OF TANZANIA'S CORPORATE BODIES: THE CASE OF PUBLIC ENTERPRISES

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Abstract

Public enterprises (PEs) have played a dominant role in Tanzania's socio-economic development. However, these enterprises have contributed significantly to economic crises presently facing the country. Precisely, they have been a fiscal and monetary burden to the economy. The main objective of this study is to analyse and make some initial attempts in assessing the magnitude of the burden. To achieve this, it became necessary to collect data of macro-nature at various focal points, namely Ministry of Finance, Tanzania Audit Corporations and various Holding Corporations. These institutions do have "consolidated", although rather scanty, data on most of the PEs.

The analysis did indicate that the public enterprises have contributed significantly in suffocating the efforts of improving Tanzania's fiscal and monetary aggregates. Consequently, the major recommendation arising from this study is the need to redefine afresh the role of public and private sector in the national economy with the ultimate objective of commercialising and privatising the public enterprises.

I. Introduction

The socio-economic policies adopted and implemented in Tanzania in the 1970s, combined with external shocks, led to economic stagnation and per capita income decline. However, this trend of affairs has been reversed since the adoption of the three-year Economic Recovery Programme (ERP) in 1986 and the Economic and Social Action Programme (ESAP) in 1989. In the course of these programmes tangible progress has been made in a number of sectors and sub-sectors. During both GDP growth averaged about 4% from 1986 to 1992. The growth of the informal sector has been quite high. The agricultural sector grew at a rate of 4 to 5% during the 1987-88 period, 6.6% in 1991 and 4.5% in 1992.

These achievements were a result of the implementation of a wide range of policies, contained in the ERP. These policies were:

1. Reduction of overvaluation of the Tanzanian shilling through nominal and real devaluation;
2. Appropriate fiscal and monetary policies;
3. Improvement of the incentive structure for agricultural production;
4. Liberalization of internal and external trade.

In spite of this wide range of measures and policies, the fiscal and monetary objectives of the programme have not been attained. The fiscal target of containing the budget deficit and monetary growth rates fell short of the planned targets. This study attributes this phenomenon to the delayed institutional reforms in restructuring the public sector, narrowly defined as the delay in reducing the size of the public sector, combined with the rehabilitation of certain key public enterprises (PEs). Consequently, the reforms would have brought about a kind of public/private sector balance that would have a more positive impact on the socio-economic development of the country. The persistence of inefficiencies and ineffectiveness in the PEs has made it difficult for the country to achieve the fiscal and monetary objectives envisaged in the ERP. The analysis of the fiscal flows reveals an overall negative impact. Thus between 1984/85 and 1994/95 there was a net transfer from the government to the parastatal sector. In real terms, the net transfers increased from Tshs. 6.3 billion in 1984/85 to Tshs.50.3 billion in 1993/94. Thereafter there was a decline to a level of Tshs.21.8 billion in 1994/95.

The main concern is the continued heavy burden of this poor performance on fiscal resources and monetary system as well as the need to reverse these trends in order to achieve internal balance and stimulate real growth. The concern about the fiscal burden

arises partly because resources have been diverted away from growth support and partly, depending on how the deficit is financed, because monetization of the growing deficit has inflationary implications. As far as the monetary system is concerned, the main concern relates to the crowding out of productive private credit and to direct credit expansion via financing of quasi-fiscal deficits. The central argument therefore, is that it does not make much sense to adopt and implement policy reforms, and thus improve the policy environment (policy formulation and implementation), without concurrently reforming the main instruments of policy: in this case the public enterprises.

The study is presented in two main sections. The first section tackles theoretical issues within the fiscal and monetary framework. The second section presents research findings on how public enterprises influence fiscal and monetary policy. In the case of Tanzania, since this influence has been more negative than positive, we therefore term it budgetary burden.

II. Theoretical framework

Tanzania's public enterprises have had a significant impact on the macro-economic performance. This is because these enterprises have been the major policy instruments used by the policy-makers to influence and direct the growth of the economy. They therefore, became the main channels of allocation of resources through budgetary allocations. It is no wonder therefore that, while there were about 42 PEs in 1967, by 1984 the number had risen to 425, an increase of 1011.9%. However, in spite of the centrality of these enterprises in the Tanzanian economy, experience has shown that the economic impact of PEs has been more negative than positive (Moshi, 1990). This is because the PEs, far from making a positive contribution to government revenue, which is one of the original objectives of state participation through intervention, have been a drain on the national budget, and have made demands on the banking system to cover their deficits, thereby reducing the private sector's access to bank credit (the crowding-out phenomenon).

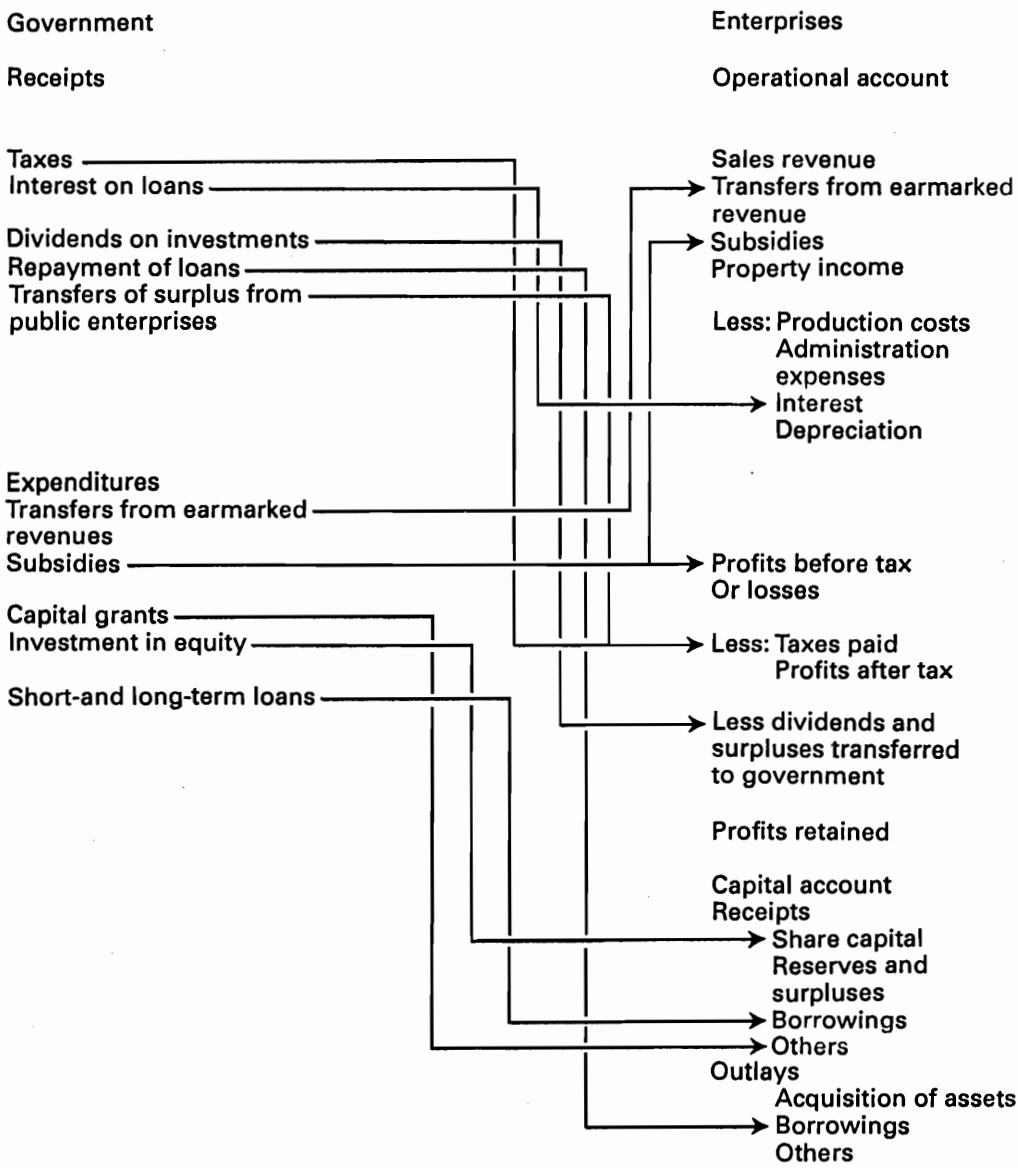
It is against this poor financial and economic performance background by the PEs and its fiscal and monetary impact on the national economy that a range of macro-economic policy reforms, which would have a strong bearing on the performance of the public enterprise sector, were introduced. These are:

- external trade liberalization, which reduced or eliminated the monoplistic protection enjoyed by many public firms;
- internal trade liberalization, which likewise allowed entry of other firms to compete with the parastatals that hitherto had monopoly positions;
- banking sector reform, which gradually required the public sector banks to take a commercial approach in lending to parastatals;
- price reform, especially exchange rates, interest rates and removal of commodity price control; and
- budget restrictions on the flow of subsidies, equity injections and other transfers to the parastatals.

It is in the context of these reforms that the need to reduce the size and rehabilitate the public sector became appreciated. This became imperative given the causality relationship existing between the size of the sector and its performance and the features of the pre-ERP Tanzanian economy mentioned above.

It is crucial to establish the budgetary linkages or relationships between PEs and the government budget. The expenditure side of the government budget is made up of flows

Figure 1: Budgetary relationship between government and public enterpriees



Source: Premchand, 1983, p. 29

to the PEs in terms of transfers, subsidies, capital grants, investment in equity and short and long-term loans. The receipts side comprises flows from the PEs which include taxes, interest on loans, dividends on investments, repayments of loans and transfers of surpluses. These relationships are illustrated more fully in Figure 1.

The fiscal impact of the public enterprise sector should, therefore, be the difference between the flows from public enterprise sector to government and the flows to the former. If there is a net flow from the public enterprises to the government, then the fiscal impact is positive, and vice versa. The impact, would be neutral if the flows in both directions cancel out (Short, 1984). If the fiscal impact is negative, then we talk of budgetary burden.

If we assume that the budgetary burden is first a product of public enterprise deficits and second that of the mode of financing of these deficits, then three possible modes of finance can be identified. First, is savings by the enterprises themselves. However, since we are talking of deficits then we assume that the enterprises concerned are not generating enough internal resource to meet their short, medium and long-term liquidity obligations as well as investment requirements. That is, their self-financing capacity is low (Moshi, 1991). Second, the government can supply finance from the budget, either through equity or subsidies. Third, the enterprises can borrow, either from domestic or international financial intermediaries, or from both.

Financing the public enterprises deficits through the second and the third modes has fiscal and monetary implications. If we consider the changes in money supply as an indicator of monetary impact, then these will depend critically on whether such finances came from either in the central bank or the commercial banks. This consideration is important in two senses. First, central bank credit to government causes money to expand directly by increasing the monetary base. Second, the monetary effects arising from finances through commercial banks will depend upon the behaviour of the money multiplier.

Related to public enterprise deficits and their modes of financing is their impact on government budget deficit on one hand and its subsequent impact on inflation on the other. However, the direct impact of government budget deficit is very much dependent upon how it was financed in the first place. A number of studies have been carried out to analyse either the macroeconomic impact of the public sector deficit (Chamley and Ghanem, 1990; Islam and Wetzel, 1990) or the financing of government expenditure and its impact on inflation (Anand and Wijnbergen, 1989). The first categories of these studies focussed on African countries, Ghana and Ivory Coast. Although these studies did not focus sharply on public enterprises per se, they concluded that, the state owned enterprise sector placed a considerable burden upon the public sector, (Chamley and Ghanem, 1990).

Apart from the issues of inflation and the mode of financing government budget deficit, the effects of devaluation on deficit is interesting for this study because of the fact that PEs have been significant borrowers from the international financial institutions. Lipumba and Noni, (1991p.3), have stated clearly that 'almost all of the (external) debt has been contracted by the public sector and guaranteed by the government. The share of the private sector in holding external debt was highest in 1973 when it accounted for 9.5% of total debt.'

The implication of this indebtedness to the government budget under conditions of devaluation is that the budget deficit is widened, unless mitigated by either inflows of external resources (and) or by rising value of exports. Even if these inflows were

forthcoming, we do strongly contend that such a situation is unsustainable in the long run.

In the Tanzanian case the analysis of the effects of ERP on a number of macro-economic indicators has been a subject of many studies. Lipumba (1990) laid emphasis on the importance of adopting an appropriate exchange rate policy as a way of improving the incentive structure and thus promote efficient allocation and utilization of resources. In another study by Lipumba and Mbelle (1990) it was found out that 'the overall deficit as a percentage of GDP is high but slightly less than 10%.' In the same study it was pointed out that the fiscal challenge facing the government was that of increasing tax revenues and contain expenditure. This recommendation was supported by the fact that the budget deficit has been increasingly dependent on external funds, something which cannot be sustained neither in the medium nor in the longrun.

As far as inflation, domestic credit expansion and monetary growth are concerned, it is found out that inflation decreased from 36.1% in 1984 to 32.4% and 31.2% in 1986 and 1988 respectively. More recent studies claim that in 1990 the official inflation rate fell to just 20% for the first time in over a decade. However, in the first quarter of 1991, inflation rose again to an average of 27.5%. The inflation estimates given here have to be interpreted with caution because they are based on an unrealistic indicator of urban dwellers' consumer price index (CPI). For example, food and transportation account for more than 68% of the CPI basket weight. Nevertheless, the estimates do indicate that the ERP's objective of reducing inflation to 20% in 1988 and to 10% in 1990 was not achieved. The ERP envisaged that the growth of money supply would oscillate around 15-20%. However, the first four years of the programme saw the money supply growing at 30%. This phenomenon explains partially the high rate of inflation in the Tanzanian economy. The persistence of this monetary imbalance is explained by the fact that 'credit by financial institutions has been allocated primarily to large parastatals, particularly to marketing institutions, often on subsidised terms (through preferential interest rates, grace periods, inadequate repayment enforcement, increasing arrears, etc). Credit to other potentially more efficient borrowers has therefore, been severely constrained and total supply response has been less than it could have been, (World Bank, 1991).

The efforts to move interest rates towards positivity have been, to some extent, fruitful. However, the lending in Tanzania's banking system, which is publicly owned, has largely been determined by government priorities and administrative allocation rather than by the economic viability and the creditworthiness of the credit demanding entities. Consequently the public sector has had the lion's share of the commercial banks' total portfolio. Conversely, the financial institutions run a huge account of 'bad and doubtful debts' because of these non-performing portfolios. This situation has brought the financial institutions to the brink of bankruptcy.

If we assume that the fiscal and monetary crisis are a product of an overexpanded, highly politicised and inefficient public enterprise sector which, over time, over-strained the government both financially and in human resources, then it is logical to argue that efforts to alleviate the crisis should, in the first instance, focus on reforming this sector. The experience of public enterprise shows that they are highly indebted, other things being equal, to the domestic banking system. This being the case, and given the high

ratios of bad debts, one cannot fail to comprehend the impact it exerts on monetary policy in general and on the banking system in particular. The failure or inability of the government to speed up institutional reforms 'will leave a legacy of unsound banking systems and large incipient financial demands on the public finances...' (Rose, and Griggs, 1990).

After having clarified a number of theoretical issues and having addressed the linkages between certain macroeconomic variables and the performance of public enterprises on one hand, and between government budget and public enterprises on the other, we intend to provide in the next section some statistical evidence to illustrate these linkages. This evidence should, therefore, provide some gross indicators of the extent of the budgetary burden.

III. The evidence

The objective of this section is to present research findings on the position of PEs in influencing fiscal and monetary process in the Tanzanian economy. The results conclude the first phase of this study and provide a basis for embarking on the next phase which will deal with the restructuring of PEs to reduce the burden of poor performance.

Public enterprises' performance

We do not intend, at this stage, either to analyse the performance of PEs in detail or to use a variety of indicators to assess such performance. Nevertheless, we are aware of studies which have used more comprehensive indicators for assessing the performance of PEs. Such indicators are the contribution of PEs to:

- Economic growth;
- Mobilisation of resources through savings;
- Employment generation;
- Income distribution; and
- Balance of payments.

Other indicators are those of capacity utilisation and the productivity of the factors of production. The main conclusion of these studies was that the PEs performance was not commensurate with the massive investments in these enterprises (Moshi, 1992). For example, the proportion of the PE sector capital formation in the year 1984 to 1995 ranged from 13.5%t to 34.5%, averaging about 22%.

We propose to use the indicator of financial performance in analysing the efficiency and effectiveness of PEs. However, we recognize the fact that financial profitability, though most desirable and necessary, does not provide an adequate measure of the efficiency of a public enterprise, given the varying and sometimes contradictory motives which led to the establishment of these enterprises. For example, the social motive of underpricing the services and products of PEs not only contributes directly to financial deficits but also increases the need for financing through credits. It is precisely because of this linkage that we argued earlier that the poor financial performance of these enterprises has been the major cause for their dependence on budgetary allocations.

Referring to the financial performances of PEs it has been observed that 'out of the 368 accounts audited, 157 annual accounts disclosed profits or excess of income over expenditure (for the commercial institutions), and 171 annual accounts disclosed losses or excess of expenditure over income (for the non-commercial institutions)' (TAC, 1987).

Although the aggregate profits made by the profit-making institutions exceed the aggregate losses of the loss-making enterprises, this is far from saying that most PEs are efficient and that profit earned is representative of the massive investments which have flown into this sector. It will be recalled that in the 1970s and 1980s the PEs accounted for 50 and 35% of fixed capital formation respectively. These percentages are quite high when compared to a weighted average of 11% for industrial countries and 27% for developing countries (Shirley, 1983).

Recent studies on financial performance of PEs during the ERP period do not indicate significant departures from past performance. In fact, the number of PEs making losses did exceed those making profits. Thus, the Tanzania Audit Corporation (1990) reports that out of the 461 accounts audited, 191 annual accounts disclosed profits (or excess of income over expenditure for non-commercial institutions) and 239 annual accounts disclosed losses or excess of expenditure. This meant, therefore, that the net losses made exceeded the net profits by Tsh 4.2 billion. The financial performance in 1991 indicates a further deterioration. Thus, net losses exceeded net profits by Tsh 4.6 billion. This being the case, it is highly questionable whether it is economically rational to continue maintaining a large public enterprise sector which in turn burdens the national budget. The PEs considered here are those owned directly by the central government. Those falling under the ownership and management of either district councils or municipalities are excluded from this discussion.

The poor financial performance of PEs leads to a fall in retained profits out of value added generated by these enterprises. For example, retained earnings declined from 39% in 1976 to 25% in 1984. This decline is nothing more than an indication of deterioration in self-financing capacity. When this capacity declines the overall domestic savings mobilization capacity of the economy is negatively affected. Consequently, the dependence of PEs on government budgets increases, a phenomenon which translates itself into an increased current account deficit. Table 1 provides a summary of profits and losses of the commercial PEs for the 1986-90 period. It is clear from the table that the relatively lower losses of Tsh 8,772.0 million in 1986 were followed by three years of higher deficits reaching a peak of Tsh 23,208.3 million in 1989. Consequently, one could argue with certainty that the financial performance of PEs during the ERP period has been quite negative, except for the positive trend emerging for the year 1990. This is not to argue that the policies of ERP were the cause of this poor financial performance. But the policies (devaluation, fiscal austerity, higher interest rates, increased competition, etc.) did aggravate the financial problems of these enterprises.

The devaluations of the Tanzanian Shilling had a strong negative impact on the foreign loans held which in turn affected the interest rate payable. Overall, from 1984 to 1995, the value of the Tanzanian Shilling depreciated at an average rate of 21.8% annually. Indeed, defaults on foreign loans guaranteed by Government increase from Tshs 696.3 million in 1984/85 to over Tshs 26 billion in 1993/94. The defaults occured mainly due

to inappropriate balance sheet structure of the PEs with excessive dependence on debt capital, the general liquidity problems facing the PEs and increases in their operating expenses. Likewise, the depreciation of the Tanzanian shilling contributed to the increase in interest payable on foreign loan balances. These rose from Tshs.6 billion in 1987/88 to Tshs.18 billion in 1993/94.

Table 1: Profits and losses of public enterprises 1986-1990 (Tsh million)

	1986	1987	1988	1989	1990
Total profits	5,964.0	14,102.5	22,408.5	32,373.7	50,436.9
Total losses	14,736.0	25,547.0	36,764.2	55,582.0	32,863.0
Overall surplus (Deficit)	(8,772.0)	(11,444.6)	(14,355.7)	(23,208.3)	17,573.9

Source: Tanzania Audit Corporation, 1992,p.12.

Public enterprises: The budgetary burden

The fiscal burden

It has been argued that the dissavings by the central government is significantly related to the failure of public enterprises to make a net contribution to the Government (World Bank, 1988). As Table 2 indicates, over the five year period ending in 1985/86, there was a net transfer on current account of only Tsh 991 million. This figure includes corporate taxes which these firms would have paid to the government even if they had been privately owned. If these taxes are excluded, there has been a net transfer from the government to PEs of Tsh 7.8 billion over this period. The very fact that very few of these enterprises remit dividends makes the situation even worse. For example, for the whole of the 1980s the dividends remitted amounted to under 7% of the total subsidies provided to the public enterprises.

The public enterprises are a budgetary burden as far as grants and subventions (generally to non-commercial enterprises) and subsidies and transfers (generally to commercial and financial enterprises) are concerned. Table 3 indicates that transfers to public enterprises rose from 6% in 1980/81 to 8.8% in 1989/90 of the gross total government expenditure

Table 2: Tanzania: Resource flows between government and parastatal sector, 1981/82–1985/86 (Tsh million)

	Dividends number remitting	Amount	Corporate taxes	Subsidies	Grants & subventions	Net transfer to government including corporate taxes	Excluding corporate taxes
1981/82	10	199.0	1,185.0	958.1	615.7	(89.9)	(1,374.8)
1982/83	9	333.6	1,348.0	–	–	–	–
1983/84	9	362.1	1,515.0	1,322.1	844.0	(498.5)	(1,844.5)
1984/85	11	406.7	1,680.0	734.4	888.5	463.8	(1,216.2)
1985/86	19	444.1	2,959.0	714.6	1,233.3	1,455.2	(1,503.8)

Source: Ministry of Finance, Treasury Registrar.

Table 3: Direct subsidies to the parastatal sector (Tsh million)

	1980/81	1982/83	1984/85	1985/86	1988/89 eat.	1989/90 prog	Average 80/1-85/6	86/7-89/90
Grants & subventions	350	845	889	1886	5137	8170		
Gross total	862	2,179	1,623	2,601	7,800	12,070		
Net total (see note below)	612	1,929	973	1,951	7,400	9,670		
Gross as % of total expenditures	6.0	11.8	6.2	8.0	7.6	8.8	8.5	8.2
Net as % of total expend.	4.3	10.5	3.7	6.0	7.3	7.0	6.8	7.0
Memo: Parastatal income tax paid	1,185	1,690	2,959	8,066	8,349			
Parastatal divideds (excl BOT)	48	92	161	350	863			
Net transfer to government (inc tax)		-341	159	519	616	-2,858	-5,024 (sum 1981/82-1989/90)	
Net transfer to governmennt (excl. inc. tax)		-1,526	-1,531	-2,440	-7,450	-1,1207	-37,089 (sum 1981/82-1989/90)	

Source: World Bank, 1991, p.40

1980/81 restructuring: NMC overdraft of Tsh 2,000 million converted to 8 years.
1984/85 restructuring: Crop authorities' arrears of Tsh 2,525 million to be repaid over 6-8 years. 1988/89 restructuring: Crop authorities' arrears of Tsh 13,642 million to be repaid over 10 years at 8% interest.
Net total refers to gross subsidies to parastatals less required payments under NBC restructurings.

Surprisingly, this upward trend continues despite the fact that explicit budgetary subsidies to commercial parastatals were abolished during the 1984/85 financial year. Even if one assumes that this increase has been a factor of non-commercial parastatals, the argument that these enterprises continue to draw heavily on the government budget is still valid. The continued access of PEs to government subsidies could be explained by the liquidity problems which is a factor of devaluation of the Tanzanian shilling, high domestic interest rates and import support schemes which require a 100% domestic cash-over from the importing entity. These factors will also account for the increased credit demand from PEs.

Table 4: Central government deficit and its contribution to monetary growth, 1982/83-1987/88.

	Money growth Tsh billion	Overall government deficit (cash)	Borrowing banks (% monetized)	Contribution to M2 (%)	Impact inflation*
1982/83	7.0	4.0	56.9	105.3	0.59
1983/84	6.5	4.5	69.5	104.5	0.59
1984/85	6.8	3.1	45.6	56.0	0.31
1985/86	8.3	5.2	62.9	72.9	0.41
1986/87	17.9	1.7	9.6	19.1	0.11
1987/88	24.5	4.5	18.2	24.1	0.13
1988/89	33.9	5.4	16.0	19.0	0.11
1989/90	24.5	0.7	3.1	2.1	0.01

Sources: Hyuha and Ndulu, 1990; Bank of Tanzania, *Economic and Operations Reports* (various issues); URT, *Economic Survey;* various issues).

* The impact on inflation is obtained by multiplying the coefficient of money supply growth on inflation, from regression estimate (Hyuha and Ndulu, 1990), by the contribution of fiscal deficit to growth of money supply.

The monetary burden

The effects of PEs on monetary aggregates are a product of, first, their contribution to increasing the government deficits on one hand and the mode of financing these deficits on the other; and, second, their borrowing propensity both from domestic and international financial institutions.

Government budget deficit

Consistent with the fiscal objectives of the ERP and agreements with IMF, net domestic borrowing by the government has been reduced significantly and was 3.8% of total expenditure in 1989/90. Consequently, the direct contribution of this deficit to money supply growth and inflation has declined. Two factors account for the decline. First, since the adoption of the ERP the demand for domestic financing of the government budget deficit has fallen significantly from 23% in the early 1980s to 7.6% in 1989/90. Second, the financing of the deficit through external sources has, conversely, increased from 18.0% in 1980/81 to 23.4% in 1989/90 (World Bank, 1991).

In spite of this apparent positive performance, Table 4 shows that money supply (M2) growth accelerated steadily from 17.5% in 1982/83 to 42% by 1989/90. The main factor accounting for this was the credit demands of the Marketing Boards and the Cooperative Unions. Their credit demands are decided outside the framework of monetary targets and thus become major determinants of money supply growth. In other words, credit to these institutions has been on the basis of politics rather than economics. Table 5 illustrates the levels of lending to these institutions for the 1984-1991 period.

Table 5: NBC: Lending to the agricultural sector 1984-1991 (Tshs million)

	1984	1985	1986	1987	1988	1989	1990	1991
Marketing Board	5,492.7	7,776.4	7,017.4	10,771. 0	24,016. 8	19,261. 2	24,158. 0	24,265. 6
Cooperatives	–	465.7	2,466.3	6,150.0	11,004. 3	15,813. 4	21,738. 0	23,479. 3
Other parastatals	423.3	529.7	1,032.8	2,014.7	2,838.2	2,628.2	3,367.1	3,367.1
Private	119.0	115.2	183.0	464.3	1,075.3	1,916.3	3,467.2	5,129.4
Total	6,035.0	8,887.0	10,699. 5	19,400. 0	3,893.6	39,619. 1	52,730. 3	56,506. 2

Source: Kimei 1991, Pg.12.

It is evident from the Table 5 that, whereas the credit demand of the marketing boards rose from Tsh 5,492.7 million in 1984 to Tsh 24,268.6 million in 1991, that of the cooperatives increased from Tsh 465.7 million in 1985 to Tsh 23,479.3 million in 1991. This meant that for the period 1984-1991 these two institutions demanded between 84.5 and 92.7% of the total credit allocated to the agricultural sector.

Public enterprises' access to credit

We noted earlier that most of the external debt which has been contracted by the public sector is guaranteed by the government. Because of these guarantees, public enterprise debt tends to be treated as sovereign debt, backed by the full faith and credit of the issuing country. Consequently, the explicit cost of this finance reflects the risk to the nation as a whole and not just the risk to enterprise (Gillis et.al., 1982). The subsequent effect of this is that as long as all financial claims against public enterprises are held by the state, the opportunity cost of funds employed in the PEs is independent of whether they are labelled as debt, equity or subsidy capital. In such a financial environment an incentive structure is created which suffocates rather than promotes efficiency, a sense of responsibility and accountability.

Of the loans issued by the Treasury outstanding on 30 June 1991, it appears that Tsh 183,651.8 million was still owed. This rose to Tsh 224,002.7 million by June 1992. The foreign component of these outstanding loans is over 54%. It should be noted that there is a heavy concentration of foreign-originated loans by a few PEs. For example, 88% of the external indebtedness is attributed to only ten industrial public enterprises out of the 70. The insolvency of these enterprises has raised the indebtedness of the country to international financial institutions on one hand, and to the domestic banking system on the other. Tanzania's external debt rose from US$ 2.5 billion in 1984 to US$ 4.6 billion by the end of 1991.

The external indebtedness, combined with the devaluation of the Tanzanian shilling, has translated itself into a high external debt service. This component of the recurrent budget as a percentage of total recurrent expenditure rose from 13.4% in 1985/86 to 23.6% in 1987/88. The implication of this indebtedness is that the government budget deficit was further widened.

Public enterprises are not only highly indebted to international financial institutions

but also to the domestic banking system. Two factors are responsible for this phenomenon. First, in Tanzania nearly all financial institutions are public sector institutions. Second, because of this, public enterprises typically enjoy a privileged access to the loans of such institutions. However, this privileged status mitigates against considerations on commercial debt capacity of these enterprises. In most cases the costs of capital do not reflect its opportunity of cost because the interest rates are administratively dictated.

The privileged access to public financial institutions has a crowding effect on private demand for credit. At the end of December 1988 the top 20 enterprises (including industrial and commercial concerns, marketing boards and cooperative unions) receiving credit from the National Bank of Commerce (NBC) represented 78% of the bank's loans over Tsh 10 million. Of that share, 19 parastatals (including the cooperative unions which have received credit allocations) received 99% of the total credit, and the other 1% went to one private enterprise. Similarly, the top 50 enterprises receiving credit represented 89% of NBC's portfolio. Forty-one public enterprises received 97% of that credit granted while nine private concerns received credit equalling 3% of the total outstanding (World Bank, 1991).

Recent studies show that there is no marked departure from the above trends. In 1987, 1989 and 1990 the public sector enterprises continued to enjoy the lion's share (84.6% 80.0% and 77.2% respectively) of the total loans and overdrafts of the NBC. (See NBC, 1989 and 1990).

If it was possible to analyse the data over the last two decades or so, it might provide a clearer picture of how this phenomenon has evolved. However, the manner in which the NBC compiles its data does not permit such a time series to be developed. Apart from the general bias against private initiative in terms of lending policy, there is the issue of disproportionate credit extension to Marketing Boards and Cooperative Unions. For example, the demand for credit by these institutions increased by Tsh 18,378 million or 109%, from Tsh 16,921 million in June 1987 to Tsh 35,299 million in June 1988. This outrageous credit expansion was due to a bumper crop harvest of cotton and maize, higher producer prices and political pressure. The ultimate effect of this was that the NBC's credit/deposit ratio rose to 146.7% against a planned ratio of 88%. As a result of this poor liquidity the bank resorted to Central Bank borrowing to bridge the gap.

The NBC is virtually bankrupt because of its failure to recover overdrafts and huge loans granted to cooperative unions, crop marketing and loss making public enterprises. Consequently, it has incurred huge losses whose exact magnitude have yet to be verified by external auditors. However, it is expected that the losses will exceed the present capital base of the bank, which is Tsh 28 billion (*Daily News*, 5 March 1992).

Table 6 Public and private access to credit

I. Access to Credit	Public # of firms	Public % value share	Private # of firms	Private % value share	Share of total NBC Portfolio
A. Total NBC Portfolio					
Top 20 borrowers	19	99	1	1	78
Top 40 borrowers	34	97	3	3	87
Top 50 borrowers	41	97	3	3	89
B. NBC Industrial and Commercial Portfolio					
Top 20 borrowers	13	82	7	18	16
Top 40 borrowers	20	74	20	26	19
Total	85	70	81	30	25

II. Contribution to Industrial Gross Output and Value Added (1983-1986).

	Industrial Gross Output	Value Added
Public Enterprises	63%	58%
Private Enterprises	37%	42%

Source: Credit data from Coopers and Lybrand Report. Data as of 31 December. National accounts from Bureau of Statistics.

The high leverage of capital structure in the PEs compared with private enterprises does not necessarily mean high risks of bankruptcy, because of the government's reluctance to allow such enterprises to go out of business. In most cases it intervenes by providing additional funds either through subsidies, the rolling-over of debt, the guaranteeing of additional external debt, or related methods. For example, in 1988 the government officially took over 40% of the liabilities of crop marketing parastatals. However, this 'bail-out' action was effected without cognizance of fiscal and monetary repercussions and without a guarantee from the concerned PEs that they will perform better in future.

The public enterprise sector lending bias is not confined to NBC alone. It extends to other financial institutions. Over 75% of the total loanable funds of the Tanzania Investment Bank (TIB) have been directed to the PEs (Moshi, 1980). However, most of these loans have been a non-performing portfolio. That is, they have not been serviced for a long time and neither payment nor solution for the inability to pay is available in the foreseeable future. As at June 1990 TIB's non-performing loans portfolio averaged Tsh 7,204.4 million. The public enterprises account for 92% of this portfolio.

Table 7: Approximate parastatal sector debt as at 30 June 1992

Source	Creditors Tsh billion	Debtors Tsh billion
Treasury direct lending (including CIS)	25	–
Treasury including from foreign sources	380	–
Tax, duties, dividends	35	–
Sub-total: due direct to treasury	440	–
Local banks (including coop unions Tsh 72 billion)	175	–
Foreign direct loans (government guaranteed)	140	–
Group loans and current acounts	85	85
Parastatal creditors/debtors (excluding banks)	80	80
Foreign trade creditors/debtors	25	15
Other creditors/debtors	55	30
Total	1000	210

Source: Haggery Olly, 1992.

The privileged access of PEs to the TIB loans, regardless of credit worthiness considerations, contributes significantly to the liquidity problems of TIB itself. Consequently, TIB maintains a huge 'provision for doubtful portfolio investments, interest and debtors'. This provision accounted for 90.8% in 1987/88, 88.8% in 1988/89 and 51.9% in 1989/90 of the total expenses (TIB, 1989 and 1990). The apparent lower rate for the year 1989/90 was caused by the fact that a number of bad debts were written off and not because of improved performance.

Table 7 illustrates the extent of the indebtedness and the sources of such finances. Apart from the already discussed fiscal and monetary implication of the high public enterprise sector debt, it has implications for the restructuring process. In fact experience has shown that massive and swift privatization is illusory where such huge debts exist. Further, delays in privatization lead to erosion of value of assets of those enterprises concerned. These and other issues will be dealt with in more detail in the proposed phase two of this study.

Conclusion

The evidence presented above corroborates with the main assumption of this study, that public enterprises have contributed significantly to the suffocation of efforts to improve Tanzania's fiscal and monetary aggregates. Although the government has restructured a number of public enterprises, like those in crop marketing and in grain trade, these efforts, however, have had an insignificant impact on the above mentioned aggregates.

In view of this, we still believe that the size of the public sector is still too big, and must be reduced urgently. The Government recently decided to review the concept of parastatals. This proposed that:

- Small public enterprises like the District Development Corporations, the Bagamoyo ranch and the Kigamboni poultry farm should be transferred from central government to their respective local government authorities;
- Viable holding public companies should be transformed into commercial agencies providing consultancy services to those who needed them, at an agreed fee;
- All business parastatals should be privatized and/or commercialized, with the question left, how and when;
- A stock market should be set up to facilitate acquisition of shares in PEs TIB, CRDB and TDFL are to work jointly on this to ensure that the market becomes operational as soon as possible;
- The Loans and Advances Realisation Trust (LART) should be set up independently of the Treasury Registrar to provide a focal point for the implementation and monitoring of the reform of the commercial parastatal sector;
- All the laws and acts guiding the activities of PEs should be amended by parliament to facilitate the implementation of the envisaged reform.

Most of these reforms have been undertaken and are at different levels of implementation. It is believed that if these reforms are successfully implemented, the burden placed by public enterprises on fiscal and monetary aggregates would be reduced significantly. Nevertheless, the success of the reforms would depend on how they are sequenced, the strength and the response of the private sector, the human and institutional capacity of the country and on the capacity of the public sector to adjust to the emerging socio-economic environment.

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Appendix

Table A1: Transfers from government to parastatals (Tsh million)

Year	Subsidies	Dividends	Parastatal borrowing requirements
1967	2.3	124.3	5.3
1968	3.1	123.4	146.8
1969	0.6	139.0	213.2
1970	14.2	157.7	154.8
1971	5.5	184.7	72.4
1972	10.3	219.2	442.1
1973	14.1	266.5	770.6
1974	90.9	331.0	969.0
1975	309.9	411.0	1.473.9
1976	61.5	597.1	1,974.0
1977	52.7	721.0	401.8
1978	97.0	871.4	1,550.8
1979	54.8	801.6	2,377.8
1980	86.1	828.0	777.1
1981	252.1	823.8	-4,362.3
1982	478.4	111.1	-6,644.8
1983	534.3	1,508.5	344.3
1984	858.3	1,825.4	532.0
1985	486.3	2,149.5	2,842.1
1986	510.5	2,981.1	-5,779.3
1987	323.8	818.1	-36,454.4
1988	463.5	1,039.0	-25,536.8

Source: Analysis of accounts of parastatals, 1990.
Parastatal Deficit = Invest less Savings (Retained Earnings)
Parastatal Borrowing Requirement = Deficit less Internal Sources of Finance
(URT) Public Sector Borrowing Requirement
= Government Borrowing + Parastatal Borrowing Requirement

Table A2: Inflation rate and money supply (Tsh million)

	Inflation	Money supply Mz (CC + DD + TD)
1967	3.0	1,539.7
1968	16.0	1,498.9
1969	16.4	1,879.5
1970	3.4	2,306.2
1971	4.0	2,713.4
1972	8.6	3,169.4
1973	10.2	3,698.6
1974	19.7	4,518.1
1975	25.9	5,615.3
1976	6.9	6,946.8
1977	11.6	8,346.7
1978	6.0	9,396.3
1979	12.9	13,806.6
1980	30.3	17,519.8
1981	25.7	20,694.7
1982	28.9	24,728.7
1983	27.1	29,127.4
1984	36.1	30,218.1
1985	33.3	38,911.0
1986	32.4	50,353.4
1987	30.0	6,642.9
1988	31.2	898,091.1
1989	29.5	92,398.6

Source: Hyuha and Ndulu, 1990
Notes: Inflation is computed as in NCPI.

Table A3: The budget deficit and sources of financing (Tsh million).

	RBS (D)	OD	DBG	GBB	GNBB	BB/DB%
1970/71	51.6	22.9	457	31.4	143	68.7
1971/72	76.6	72.2	289	174	110	60.2
1972/73	181.1	56.9	186	6	180	3.2
1973/74	237.9	(19.8)	717	521	196	72.7
1974/75	(15.2)	(23.7)	1196	834	362	69.7
1975/76	202.9	(10.7)	906	570	336	62.9
1976/77	1,426.5	(1,734.4)	308	–	309	–
1977/78	518.8	(5,501.5)	3,511	3,057	717	24.0
1978/79	(1,471)	(6,296)	3,075	2,804	671	91.2
1979/80	(1,264)	(6,412)	4,279	3,464	814	81.0
1981/82	(2,254)	(7,181)	4,061	3,278	783	81.0
1982/83	(1,727)	(6,412)	4,279	3,465	814	81.0
1983/84	(2,715)	(6,903)	4,797	4,009	788	83.6
1984/85	(2,194)	(19,871)	4,435	3,310	1,125	75.0
1985/86	(5,891)	(9,678)	6,231	4,925	1,306	79.0
1986/87	(4,622)	(18,549)	4,514	1,656	2,858	37.0
1987/88	(11,432)	(27,818)	2,236	236	2,000	10.5
1988/89	–	(35,681)	7,146	4,460	2,686	62.0
1989/90						
1990/91						

Sources: Economic Survey; BOT Economic and Operations Reports
RBS (D) = Recurrent Budget Surplus (Deficit)
DD = Overall Deficit
DBG = Domestic Borrowing by Government
GBB = Government Bank Borrowing
GNBB = Government Non Bank Borrowing
BB/DB% = Bank Borrowing as 9% of Domestic Borrowing

Table A4: Performance of commercial parastatals (Tsh million)

	1984	1985	1986	1987	1988
Total profits	3,799.0	6,964.2	5,949.2	14,095.6	19,857.1
Total losses	2,437.7	2,829.6	14,735.5	25,544.0	35,131.1
Aggregate surplus/(deficit)	1,361.3	4,134.6	(8,786.3)	(11,448.4)	(15,274.0)
Total surpluses	81.3	106.8	131.3	204.5	367.7
Total losses	215.5	401.4	211.7	147.6	512.3
Net surplus/(deficit)	(134.2)	(294.6)	(90.4)	56.9	(144.6)

Table A5: The budget, banking, financing and the money supply (Current Tsh billion)

	1983/84	1984/85	1985/86	1986/87	1987/88	Cumulative Total
1. Budgetary Expenditures	23.9	26.7	33.2	55.5	76.9	216.2
2. Commercial Bank Lending and Interest Payments	1.5	2.7	0.2	15.5	28.6	48.4
3. Adjusted Revenues (1+2)	25.4	29.3	33.4	71.0	105.5	264.6
4. Budgetary Revenues and Other Items	16.1	19.7	24.0	42.7	55.8	158.3
5. Interest payments to Public Entities	0.1	0.3	0.6	-0.2	2.5	3.3
6. Non-Bank Deficit Financing	3.4	3.8	4.2	11.5	20.2	43.1
7. Adjusted Revenues (4 + 5 + 6)	19.6	23.8	28.8	54.0	78.3	204.7
8. Financing Gap (Residual) Monetary Financing (3-7)	5.8	5.5	4.6	17.0	27.0	59.9
9. Actual Increase in Money Supply	1.1	8.8	11.4	16.1	23.4	60.8
10. Memo: Conventional Budget Deficit Residual Financing						14.8

Source: World Bank, 1991, p.45.

Table A6: Money supply and inflation

	1984	1985	1986	1987	1988	Average 1985-88
Money supply[1]	3.7	29.0	29.0	32.0	36.7	31.7
GFDP Growth Predicted Inflation[2]	3.4	2.6	3.1	4.0	4.5	3.6
Actual Inflation	36.1	33.3	32.4	29.9	28.2	30.5
Ratio Predicted/ Actual Inflation	0.01	0.80	0.81	0.94	1.14	0.92

Source: World Bank, 1991, p.46.
[1] Currency outside banks plus banks deposits.
[2]Percentage increase in Money Supply minus growth rate. Velocity of circulation assumed to remain constant.

Table A7: Capital account: parastatal enterprises (Tsh million)

Item Receipts	1976	1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Retained Profits	811.10	1,292.50	524.60	2,612.80	2,393.20	4,063.50	1,554.10	6,460.10	2,449.30	14,992.60
2. Depreciation Provision	240.20	907.40	1,191.70	1,165.50	1,381.80	1,558.10	3,115.10	4,528.30	9,629.30	12,885.50
3. Loans from Tanzania Govt.	431.60	76.80	119.60	979.50	446.80	426.50	603.80	100.20	3,0318.90	52,315.30
4. Grants from Tanzania Govt.	332.50	512.20	707.80	712.80	2,188.30	1,980.10	1,625.10	1,186.00	2,581.40	2,818.60
5. Loans from abroad	189.60	714.70	1,089.70	9,591.70	1,794.00	1,377.50	2,865.20	4,965.50	39,940.90	9,593.70
6. Grants from abroad	164.80	133.40	273.40	178.80	388.40	285.90	2,149.10	1,758.50	1,925.60	2,985.40
7. Local Borrowing	2,823.40	2,657.10	5,386.30	1,545.20	2,774.10	1,951.40	8,413.00	11,675.40	33,474.30	34,062.10
8. Other source & cash balance	-446.50	6,102.70	550.70	-750.80	-6,770.80	-303.60	5,841.60	36,873.80	-11,512.70	113,029.30
9. Total	4,546.70	12,396.80	9,843.80	740.50	4,595.80	11,340.20	26,167.00	69,347.80	108,807.00	242,682.50
10. % of 3 9	9.5	0.6	1.2	13.2	10.4	3.8	2.3	0.1	27.9	21.6
11. % of 4 9	7.3	4.1	7.2	9.6	47.6	17.5	6.2	1.7	2.8	1.2
12. % of 5 9	4.2	5.8	11.1	13	39	12.1	11	7.2	36.7	4
13. % of 7 9	62.2	21.4	54.7	20.9	60.4	17.2	32.2	16.8	30.8	14
14. % of (3 4) 9	16.8	4.7	8.4	22.8	58	21.3	8.5	1.8	30.7	22.8
15. % of (5 + 6) 9	7.8	6.8	13.8	15.4	47.5	14.7	19.2	9.7	38.5	5.2

Source: Analysis of accounts of parastatals, 1991.

Table A8: Interest rates paid by public enterprises for loans from the treasury

Interest Rate	Frequency
0	64
0.75	5
1	5
1.25	1
1.5	1
2	5
2.5	4
3	5
3.5	1
3.55	1
3.87	1
4	18
4.5	1
5	13
6	6
6.75	3
7	5
7.25	1
7.5	5
7.9	1
7.5	1
7.92	1
7.95	1
8	9
8.4	3
8.5	4
9	3
10	35
11	5
12.5	1
14	4
14.5	2
15	3
20	1
21	1
22	
5	
5	
1	
5	
1	

Source: Author's computations.

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