

**DEBT RELIEF AND POVERTY REDUCTION IN TANZANIA**  
**Prospects and Challenges**

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Paper to be presented at the 1<sup>st</sup> IFMASA Workshop on Poverty Alleviation and the  
Financial Management System in Tanzania  
IFM Function Hall, Dar es Salaam, Wednesday, November 29<sup>th</sup> 2000.

The usual disclaimer holds. That is views expressed in this paper are those of the author  
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## 1. Introduction

Although the debt and poverty issues of developing countries appear to be at the top of the agenda in international and national forums since the early 1980s it has become increasingly clear that the external debt situation of Sub-Saharan Africa (SSA) countries including Tanzania is one of the more severe of the many obstacles to growth and development in the region (Styme, 1990). It was also observed that the external debt burden in SSA was growing amid mounting evidence of widespread poverty (Nyerere, 1999). In Tanzania for example, it is estimated that while the per capita debt has grown from over US \$ 180 in 1989 to US \$ 236.5 in 1999 the poverty stance had also deteriorated. Based on the 1991/1992 Household Budget Survey, around 27 percent of the people were in households with total expenditures that was insufficient to obtain enough food to meet nutritional requirements, and about 48 percent of the households were unable to meet their food and non-food basic requirements. The results of various updated estimates for year 2000 suggest those poverty levels may have increased to over 50 percent for Mainland Tanzania (URT, 2000, pp.4-5).

There is yet another dimension of the debt problem which is directly or indirectly connected to the poverty problem. That is, at the time the debt problem is mounting the terms of trade have moved against LDCs products.<sup>1</sup> At the same time, adverse weather conditions and other production constraints in developing countries have meant a significant decline of agricultural output. The terms of trade and output effects have intertwined to produce a negative income and growth effects in most debt-ridden countries. It is such effects that are commonly associated with poverty.

Given this background it is clear that unless indebted countries are assisted to deal with their poverty status they cannot repay the loans. That is the reason why various proposals and strategies have been initiated by bilateral as well as multilateral creditors with a view to addressing the debt and poverty problems of Less Developing Countries.<sup>2</sup> According to some researchers the Highly Indebted Poor Countries (HIPC) Initiative proposed jointly by the International Monetary Fund and the World Bank in 1996 is (arguably) the most recent and comprehensive

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<sup>1</sup> See International Financial Statistics, 1990, 1995 and 1998, UNCTAD, Direction of Trade Statistics, Various

<sup>2</sup> The London and Paris Club arrangements are examples of such initiatives.

approach to LDCs poverty and indebtedness problems.<sup>3</sup> By agreeing to institute the (HIPC), International Financial Institutions have finally realised that the indebted countries like Tanzania cannot repay their external debt obligation unless their poverty stance is addressed.

This paper uses the case of Tanzania to examine the prospects for external debt relief under the HIPC initiative and challenges ahead of the country as it attempts to address the seemingly widespread poverty problem. The point of departure, which is dealt with albeit briefly in section two of this paper, is an overview of the theoretical linkage between foreign indebtedness and poverty. The trend and magnitude of poverty and external debt in Tanzania are discussed in section three while the prospects and challenges for debt relief and poverty reduction are discussed in section four. Finally in section five some concluding remarks are made.

## **2. The External Debt-Poverty Nexus: Some Theoretical Linkages**

Most development models especially those which descend from the Harrod-Domar tradition treat external debt like other externally generated resources such as aid whose purpose is to fill resource gap (either saving or foreign exchange) assumed to exist in most capital-deficient countries (Chenery and Strout, 1966). These models posit among other things that when efficiently used, external debt resources have the potential to improve the productive capacity (and the production possibility frontier) and help to put the borrowing country in a sound economic footing in such a manner that when time for repaying the loans comes its growth prospects are not jeopardised.

However, if the external loans are unproductively used by the borrowing country for example in investment undertakings that are of questionable economic rationale, the end-result may be a contraction of the production possibility frontier when consideration is given to the fact that the repayment of the loans imply a leakage of the resources away from a borrowing country.

The literature that treats the link between poverty and indebtedness often focuses on the so-called “vicious circles of poverty” (see for example Crumm, 1985, Danielson and Mjema, 1987). It is argued in such circles that poor countries are poor because they lack capital and other essential ingredients needed for development. It is further argued that

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<sup>3</sup> See, among others, Sarbib (1997)

such (poor) countries can not borrow capital from capital-rich countries because of low credit-worth stance which is, in turn, a result of their failure to repay long term outstanding external debt obligations (Mjema and Kilindo, 2000).

Another category of literature analyses the debt-poverty nexus from the terms of borrowing perspective. There is a body of literature, which tend to support the view that indebtedness has enhanced poverty in most debtor nations due to the “hardening” borrowing terms. Thus, it is claimed in this literature, that not only has the volume of lending from rich to poor countries considerably declined over time but also the terms of borrowing have tended to harden. According to Table 1 there is evidence that the borrowing terms like average interest on loans, average maturity period and the average grace period have all moved against LDCs especially those in SSA in general and for Tanzania in particular.

Table 1: Trends in Terms of Loan Borrowing for LDCs: 1961-1999

	AMP*				AGR*				AIR*		
	LDCs	SSA	Tz		LDCs	SSA	Tz		LDCs	SSA	Tz
1961	20	25	30		4	6	4		4	6	4
1970	18	18	39		5	6	4		5	6	4
1974	16	17	29		5	6	10		6	5	4
1978	14	16	30		4	4	7		7	6	4
1982	14	18	28		4	4	7		10	8	4
1985	13	17	24		4	4	7		8	7	4
1988	12	14	21		4	4	7		8	7	4
1990	11	12	17		4	4	6		9	8	4
1995	10	12	17		4	4	6		10	9	4
1998	10	11	16		4	4	5		10	9	4
1999	10	11	15		4	4	5		11	9	4

Notes: AMP\* = Average Maturity Period (years)

AIR\* = Average Interest Rate (%)

AGR\* = Average Grace Period (%)

Source: World Bank, World Debt Tables, various.

The hardening of loan borrowing conditions imply among other things that scarce foreign exchange resources needed in LDCs will have to be used for servicing the debt.

### **3. Indebtedness and the Poverty Stance in Tanzania: An Overview**

#### ***3.1 The External Debt Situation***

In Tanzania, external indebtedness became a serious problem since the mid 1970s (Lyakurwa, 1984, Mjema and Kilindo, 2000). In 1970 for instance it was estimated that about US \$265m worth of external debt resources were disbursed to Tanzania. That amount increased almost five fold to US \$ 1338m in 1980. Between 1980 and 1990 the country's foreign indebtedness almost quadrupled from US \$ 1338 m to US \$4987 m. There was little slowdown in growth of debt between 1990 and 1998 but the level reached around US \$ 8,000 in 1998.

The total debt outstanding to Tanzania has been predominantly official (i.e. multilateral and bilateral debt). Throughout the 1990s for example the official debt made over 90 percent of Tanzania's total outstanding debt. Further decomposition of official debt shows that the share of bilateral debt in total debt has been changing. In 1990 for example it was about 60.1 percent while multilateral debt was 31.3 percent of total debt.

As foreign indebtedness increased, so did the servicing of the debt. In 1974 Tanzania used a total of US \$23.4 m to service its debt. This amount increased to US \$51.2m by 1980 and to US \$73m in 1989. By 1990 debt the amount of money used to service Tanzania's debt increased to US \$ 218.7m. Throughout the 1990-1999 period, the debt service amount has averaged at over US \$ 250m annually.

In comparison with other SSA countries and, using the external debt -to-export and the debt to Gross National Product one can observe that Tanzania qualifies to be in the debt distressed group of countries. This has, in turn, implied that the government's ability to finance its plans including social services is severely limited

Table 2: Structure of External Debt in Tanzania, USD million and percent

	1994/95	1995/96	1996/97	1997/98	1998/99	1999/2000
Total Debt	8,440.7	7,933.0	8,100.8	7,901.7	7,972.9	7,802.6
Disbursed debt	6,917.5	6,623.3	6,600.3	6,435.8	6,580.3	6,509.6
Disbursed by creditor (percent of disbursed debt)						
Bilateral debt	49.5	48.6	46.1	43.6	42.5	38.8
Multilateral debt	43.7	45.1	47.6	49.3	50.6	53.7
Commercial debt	3.3	3.2	3.3	4.0	3.8	3.9
Other private creditors	3.5	3.1	3.0	3.1	3.0	3.6
Debt by borrower (percent of disbursed debt)						
Central government	94.3	94.6	94.4	93.5	93.7	80.8
Public corporations	3.2	2.6	2.5	2.7	2.5	15.9
Private sector	2.5	2.8	3.0	3.8	3.8	3.3
Disbursed by use (percent of disbursed debt)						
BOP support	27.3	25.5	23.1	23.2	23.0	18.7
Transport	19.2	19.5	20.3	20.3	20.3	21.5
Agriculture	14.7	14.6	14.4	14.2	14.6	15.6
Energy and mining	10.0	10.9	11.3	12.3	12.5	13.2
Industries	9.5	9.2	8.6	8.2	7.7	7.8
Social welfare	3.2	3.7	3.9	4.3	4.4	4.9
Finance and	3.1	2.9	2.8	2.6	3.3	3.7
Others	11.8	12.3	14.2	13.7	12.9	13.5
Memo:						
Debt Ratio (%)	190.52	147.89	140.48	106.9	109.06	n.a.

Source: External Debt Department, Bank of Tanzania.

According to Table 2 the external debt resources have been used to finance things like balance of payments support, transport, agriculture and energy and mining.

#### 4. Prospects and Challenges Ahead in Targeting Poverty and Indebtedness

There appears to be a general consensus among bilateral and multilateral donors that the 'fight' against poverty needs to be approached from a multi-sectoral dimension. The World Bank and the International Monetary Fund have made it a condition that debt relief resources realized from the HIPC initiative must be used by indebted governments qualifying for this initiative in promotion of social service delivery capacity and in programmes that benefit the poor.

In response to this condition, the Government of Tanzania has prepared a strategy – the Poverty Reduction Strategy Paper (PRSP). The government of Tanzania maintains that the PRSP is based on three broad considerations (URT, 2000 p. 12).

(a) it is an instrument for channelling national efforts towards broadly agreed objectives and specific inputs and outputs.

The implementation of the strategy is an on-going process. The ultimate aim of the strategy is to shift the responsibility of formulating, implementing and monitoring poverty reduction to districts and municipalities at the grassroots level. The strategy will need to be managed in a flexible way so as to accommodate additional action plans and activities emanating from the on-going work.

(b) the poverty strategy is viewed as an integral part of the macroeconomic structural reforms that are being supported by Tanzania's multilateral and bilateral partners and;

(c) in keeping with the concerns of the stakeholders, and guided by the overarching orientation of Tanzania's long term development plan the focus of the poverty reduction strategy concentrates on efforts aimed at reducing income poverty, improving human capabilities, survival and social well-being and containing extreme vulnerability among the poor.

There is evidence to link economic growth and the poverty stance of a country. Indeed the PRSP recognises economic growth as a powerful means of reducing income poverty. For income poverty to be reduced, the rate of GDP growth has to be accelerated and equity promoted.

The government will have to continue to maintain sound economic policies and intensify the implementation of reforms aimed at market efficiency and factor productivity.

Furthermore budgetary expenditure will continue to be restrained for macroeconomic consideration purposes. At the same time the government needs to support programmes and social services under the poverty reduction strategy. Furthermore efforts including those aimed at promoting private investments needs to be made to raise steadily the investment ratio from 15 to 17 per cent thereby encouraging cultivation of new crops, small and medium size enterprises and informal sector activities.

Although in the past there have been attempts by the creditor and donor community to address the debt problem of LDCs, the current additional in the arsenal of approaches to indebtedness is the HIPC initiative<sup>4</sup>. According to the World Bank and the IMF the (HIPC) Initiative is based on six principles; i.e.;

- (a) the objective is to target overall debt sustainability on a case-by case basis but focusing on the totality of a country's debt.
- (b) Actions should be envisaged only when the debtor has shown, through a track record, ability to put to good use the exceptional support provided
- (c) The new measures should be built, as much as possible on existing (debt relief) mechanisms
- (d) Additional action should be coordinated among all creditors involved, with a broad and equitable participation
- (e) Action by multilateral creditors should preserve their financial integrity and preferred creditor status, and
- (f) New external finance for the indebted countries should be on appropriately concessional terms.

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<sup>4</sup> For a comprehensive analysis of the HIPC initiative see Sartib (1997).



Like governments of other highly indebted poor countries, the Tanzanian government has welcomed the (HIPC) initiative and has made preparations to ensure that the debt problem is addressed adequately. The country's National Debt Strategy (NDS) for example recognizes the need to build on existing debt reduction strategies and aims at:

- (i) restoring orderly relations with all creditor with a view to settling all arrears or repayment and preventing the increase in outstanding debt
- (ii) reducing contractual debt service due to a manageable level of about 20 percent of debt service ratio
- (iii) preventing the build-up of an unsustainable level of debt and debt servicing in future.

The government has also identified key areas (including education, health and water) where the debt relief money needs to be spent to have a maximum effect on poverty reduction.

The HIPC initiative has however three distinctive features, which distinguishes it from earlier attempts which deals with and targets total (multilateral and bilateral) debt. Secondly, for the first time there appears to be recognition of the linkage between increasing indebtedness and widespread poverty. The International financial institutions have finally recognized that widespread poverty in indebted countries is a constraint to their ability to service the debt. Finally the initiative introduces an important aspect of good governance by insisting on a consultative approach to the debt problem involving the creditor community, the concerned governments and the private sector including non-governmental organizations.

Table 3 shows the amount of debt relief with and without the HIPC initiative.

Table 3: Debt Servicing After HIPC Relief (US \$ m, and % respectively)

	99/00 <sup>a</sup>	00/01	01/02	02/03	03/04	04/05
Total debt	235.5	153.3	141.8	143.8	148.5	158.2
Service <sup>b</sup>						
Principal	167.4	97.5	82.3	80.4	81.4	81.4
Multilateral	83.2	47.8	30.2	25.9	42.2	53.9
Official bilateral	79.9	43.5	45.5	49.9	36.3	27.4
O/w: Paris club	61.4	23.1	28.2	31.0	24.6	23.3
Commercial	4.3	6.7	6.7	6.7	3.4	0.0
Interest	66.2	26.3	63.4	66.6	70.4	74.5
Multilateral	19.9	13.3	10.3	8.6	9.1	9.1
Official bilateral	43.4	33.4	38.8	37.3	35.9	35.1
Paris club	39.5	27.3	30.2	32.4	31.6	30.9
Commercial	1.0	1.5	1.1	0.7	0.4	0.1
New debt	3.1	8.0	12.3	16.8	21.2	25.5
Total debt service <sup>c</sup>	295	317.8	310.9	362.7	258.8	259.0
Debt service ratio <sup>c</sup>	24.8	24.6	20.9	25.6	13.7	12.5
Debt service ratio <sup>b</sup>	19.8	11.9	9.5	8.4	7.8	7.3

Source: IMF/IDA (2000), Table 12.

Notes: <sup>a</sup> Estimates

<sup>b</sup> After HIPC relief

<sup>c</sup> Before HIPC relief

The real challenge is whether the HIPC initiative, the National Debt Strategy, the Poverty Reduction Strategy Paper and other strategies that are in the process of being formulated will actually be able to adequately alleviate poverty and address the indebtedness problem facing the country.

Table 4: Tanzania Selected Macroeconomic Performance Indicators: 1988-1998

INDICATOR	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998
Real GDP growth (%)	4.4	2.6	6.2	2.8	1.8	0.4	1.4	3.6	4.2	3.3	4.0
Domestic saving (% of GDP)	16.5	18.1	26.1	26.3	27.2	25.1	24.6	19.8	16.6	14.9	15.0
Inflation	31.8	30.3	35.8	28.7	21.8	24.0	33.5	27.4	21.0	16.1	12.9
External Debt (% of GDP)	167.1	127.9	159.7	150.5	141.5	156.1	178.4	128.7	101.0	90.2	88.1
External Debt Service (% of GDP)	10.8	9.6	10.2	8.9	8.5	14.4	15.5	11.2	9.8	6.6	6.3
External Debt Service (% of exports)	83.6	70.8	76.6	70.4	62.2	88.2	61.9	44.8	46.6	36.9	36.4

Source: Calculated from Economic Survey.

Specifically however the tasks ahead of Tanzania are to ensure:

- (i) a growth rate of about 5.5 percent per annum during the 2000-2002 period and about 6% thereafter. These projects are conditional on improvement in infrastructure, normal weather and continuation of economic liberalization and public sector reform.
- (ii) A growth in traditional export sector of between 4-6 percent per year and a growth in the non-traditional sector of more than 6 per cent.
- (iii) A substantial growth in foreign direct investor. This is important because in Tanzania today the financing gap remains large and is covered by continuing high inflows of overseas development assistance.

Table 5 shows some trends in selected macroeconomic indicators in Tanzania since 1970.

Table 5: Selected Macroeconomic Indicators in Tanzania: 1970-1999

Year	GDP Growth (%)	Debt Growth (%)	Export Growth (%)	Population (m)	Per capita income Tsh	Per capita income growth (%)
1970	-	-	-	13.27	34,251.31	-
1971	4.1	22.9	16.0	13.63	34,740.49	1.4
1972	6.7	22.9	16.0	14.00	36,097.28	0.4
1973	3.0	26.8	7.0	14.37	56,242.10	0.4
1974	2.5	43.1	15.6	14.76	36,166.59	0.2
1975	9.4	29.5	1.8	15.31	38,156.6	5.5
1976	2.9	42.0	53.0	16.41	36,653.3	3.9
1977	0.3	32.1	10.0	16.92	35,690.3	2.6
1978	2.1	12.1	16.0	17.44	35,131.20	0.9
1979	2.4	10.0	4.8	17.98	35,013.34	0.65
1980	4.5	12.7	7.9	18.58	35,013.34	0.33
1981	0.5	7.6	8.1	19.77	33,764.78	-3.5
1982	0.5	9.3	-11.7	19.17	33,764.7	-0.33
1983	-2.3	10.6	3.0	19.79	32,900.65	-2.5
1984	3.3	2.9	41.3	20.41	31,148.55	-5.3
1985	4.5	13.0	-1.6	21.06	31,202.84	-2.5
1986	1.8	14.0	88.2	21.73	31,629.08	-5.3
1987	4.9	19.7	107.7	22.48	31,197.87	0.17
1988	4.0	5.1	65.1	23.22	31,646.38	1.3
1989	3.9	-1.0	47.3	23.89	31,646.38	-1.4
1990	4.4	14.5	45.7	24.57	33,787.47	1.4
1991	5.7	17.0	6.3	25.27	33,285.55	1.5
1992	3.5	1.7	52.8	25.99	33,817.37	2.7
1993	4.1	1.6	82.0	26.73	34,746.97	0.65
1994	3.0	7.9	52.7	27.49	34,976.10	1.2
1995	3.5	5.3	53.4	28.28	35,490.79	0.18
1996	4.5	-5.9	3.2	29.09	45,328.99	0.6
1997	3.5	-1.1	-1.2	29.98	66,656.03	1.2
1998	3.9	3.0	4.1	30.91	77,140.07	0.2
1999	4.0	2.5	30.2	31.24	80,131.45	2.8

- Sources:
- (i) Economic Survey, various, Planning Commission.
  - (ii) BOT Debt Profile of Tanzania.
  - (iii) Own calculations.

## 5. Concluding Remarks

This paper has briefly outlined the prospects and challenges ahead as Tanzania deals with debt relief and poverty reduction. While the prospects for debt relief under the auspices of the HIPC initiative are real, the magnitude of the poverty problem is threatening. Given this background it is important for the country to:

- (i) develop an efficient debt management strategy.

The country should be able to develop an alternative debt strategy which convinces the creditor community that what Tanzania is aspiring for is a total debt cancellation and not debt rescheduling. The alternative strategy debt strategy should clearly show how debt cancellation will assist countries like Tanzania to address the debt problem but also deal effectively with the poverty problematique. In this way these countries may be systematically integrated into world economic.

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