LIBERALISATION OF THE BANKING INDUSTRY IN TANZANIA:

Issues and Prospect

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ABSTRACT: In Tanzania, as in many other developing countries, banks play a predominant role in the financial sector of the country as far as mobilisation and allocation of financial resources is concerned. The question that deserves attention however, is whether and to what extent foreign banks have been playing a positive role in the promotion of the country's economy. Looking at this concern the paper notes that after the enactment of the Banking and Financial Institutions Act, 1991 the banking industry has undergone a dramatic change allowing the establishment of private banks in the country.

On the one hand the liberalisation of this sector has made it possible for over 800 Tanzanians to get employed in sixteen projects which were approved up to 1998 by the government authorities to carry on financial business, mainly in the banking sector. On the other hand the Bank of Tanzania reveals that the sector has contributed to the country's GDP by an average of 4.0 percent between 1990 and 1996. This paper discusses the role that has been played by the banking system especially after the arrival of private investors in the sector. Various issues and prospects in the industry are examined.

INTRODUCTION

Banks[1] hold a unique position in most economies as creators of money, the principal depositories of the public's financial savings, the primary allocator of credit, and managers of country's payment systems. Tł therefore perform an intermedi: function as gatherers of deposits a allocators of credit. It is through tl function that banks, in one way another, contribute in the financial grow of the country. According to Kir (1987) financial growth - characterised l an increase in the number and variety financial institutions both bank and nc bank institutions[2] and a substantial rise

[1] The term "bank" is used in this paper as a generic term covering all types of deposit and credit institutions.

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[2] For the list of banks and non-financi Institutions see Appendices I and II.

the ratio of total financial assets to gross national product (or tangible wealth) - is a necessary condition for rapid economic growth.[3]

The banking system in Tanzania has a long history from the colonial era to the times of socialism regime and now to the market oriented economy. There have been changes in the sector after the enactment of the Banking and Financial Institutions Act 1991 whereby the state owned banks have been restructured and the private banks licensed to carry out the banking business.

From the general perspective, this paper looks at the banking system and appraises the impact of the sector to the Tanzanian economy. While this section gives an introductory note, section two looks, albeit briefly, at the historical background of the banking system in Tanzania; both prior and post Arusha Declaration as well as after the enactment of the BAFI Act in 1991. Furthermore, this section will also deal with the current composition of the banking system. The remainder of this paper is organised as follows: Section three deals with the legal aspects regarding licensing as well as regulating the banks. In this section the paper proposes for creation of an effective framework of prudential regulations. Section four deals with the supervisory intensity by the central bank and proposes a working matrix for supervisory purposes in order to have a system of corporate governance. Section five deals with the contribution of these banks to the economy. In this section, among other things, the paper looks at the banks' performance with respect to deposit mobilised and credits extended to the public particularly in the period 1988-1997. Finally, section six of the paper provides some concluding remarks.

HISTORICAL BACKGROUND

The financial system[4] in Tanzania has passed a long way from the colonial era up to now. At the time of independence branches of foreign commercial banks comprising Standard Bank of South Africa, National and Grindlays Bank and Barclays Bank D.C.O dominated the banking system. Other smaller foreign banks which were in operation in the country included: Ottoman Bank (1958), Bank of India (1953), Bank of Baroda (1953), Commercial Bank of Africa (1961) and National Bank of Pakistan (1962) (see Bank of Tanzania, 1996).

Historically these banks were established locally to finance external trade rather than develop local activity. However, the effect of their establishment was able to stimulate at least certain sectors of local enterprise as traders and settlers deposited the proceeds of exports in local accounts or imported foreign capital (Livingstone and Ord, 1980). Non-bank financial institutions were Post Office Savings Bank, foreign insurance companies and three specialised agricultural credit institutions initiated by the colonial governments namely the Land Bank, the Local Development Loan Fund and African Productivity Loan Fund.[5]

In 1967, after the Arusha Declaration, all financial institutions were nationalised and put under the control of the government. For instance, the

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[3] See Shaw (1973), McKinnon (1973) and Nkoba (1997).

[4] In this paper the terms "financial system" and "banking system" are used as synonyms.

[5] See Bank of Tanzania (1996).

commercial banks were all merged into one bank, "The National Bank of Commerce (NBC)" under the NBC Act 1967 (Establishment and Vesting of Assets and Liabilities). It was hoped that a nationalised banking system, by applying social rather than private profitability criteria, would transcend the limitation of the foreign banks and attain, inter alia: (a) rapid extension of banking facilities throughout the country; (b) a fairer remuneration of deposits; and hence, with (a) above, an accelerated rate of savings mobilisation; (c) efficient distribution of the savings mobilised through the banking system according to national priorities; and (d) modest profit for the government. The banking sector eventually became a monopoly one. The capacity of a monopoly bank to reach these expectations depends largely on its legal standing and the type of control exerted over it by the monetary authorities (the central bank and the treasury). Unexpectedly the banking sector performed poorly, partly because of undue government interference and partly due to the ineffective banking legislation that was in operation at that time.

In 1991 an Act was enacted to consolidate the law relating to banking and harmonise the operations of all the financial institutions in Tanzania. It was, and still is, expected that the Act will foster sound banking activities, regulate credit operations, and provide for other matters incidental to or connected with those purposes. Up to 1993, however, the banking system consisted entirely of insolvent and inefficient government-owned banks. The largest being the National Bank of Commerce which for instance accounted for 90 percent of commercial bank deposits and the Co-operative and Rural Development Bank which accounted for five percent of the sector. The balance in the banking sector consisted of the People's Bank of Zanzibar (PBZ) ar the now defunct Tanzania Housing Bar (THB).

The sector later on permitted tl entry of private banks. The early entran included Meridian BIAO and Standa Chartered.[6] Today the banking system Tanzania consists of twenty banks ai nine non-bank financial institutions.

THE LEGAL ASPECTS: LICENSING AND REGULATING THE BANKS

Before the nationalisation of ban in 1967, the law that govern banking business in the coun was the Banking Ordinance (Ca 430 of the Laws in Tanzani Unfortunately this law could not susta all the changes that had to be made in t banking system after the Nyira commission. Following t recommendations of the commissior new Act was enacted in 1991 to look i all matters relating to banking business the country.[7] It gives the power to central bank of this country to license a regulate all the banks doing the busin of banking in the country.

For a stable banking system a bro body of legislation is essential to ens that the central bank (supervisors of banking system in the country) can ca out and enforce their responsibilities Tanzania and most other countries, legal framework applicable to ba encompasses prudential laws regulations, the laws govern commercial transactions and (

6 Meridian BIAO, however, collapsed in and was taken over by Stanbic Bank Ltd

7 See BAFI Act No. 12 of 1991.

recovery, and bankruptcy laws. When an appropriate framework does not exist, it is a significant contributor to banking sector problems.

It is in the same spirit that Section 51(1) of the BAFI Act 1991 requires the governor of the central bank to make regulations for carrying out or giving effect to the purposes and provisions of the Act. The two main goals that regulation of the banking sector aims to achieve are: (i) to protect individual investors; and (ii) to ensure the stability of the financial system. Regulation is needed because of the possible market failure owing to information problems, externalities, or problem of market power. The primary reason why the individual investor has to be protected is that the financial sector is based on trust--the system only works because enough people have sufficient confidence that it works--and that fraud is always a possibility. Regulation might also protect the depositor from abuse of market power by banks, and the deregulation and liberalisation of financial markets may make this issue more important (Chari and Jagannathan; 1988). However, according to Van Damme (1994) one cannot be sure that regulation is not free from side effects; it is difficult to guarantee that regulation of one type of inefficiency does not introduce another inefficiency somewhere else in the system.

This paper looks briefly at the key regulations that have been issued by the Bank of Tanzania in compliance to Section 51(1) of the 1991 Act. The regulations are: licensing or criteria for entry, prudential regulations, capital adequacy regulation and asset diversification.

Licensing or Criteria for Entry

Since most banks, especially the small ones, fail because of poor management and connected lending, the initial decision to grant a license is an important one.[8] The banking law in the country recognises this fact and Section 4 of the 1991 Act prohibits any person other than a bank to carry on the business of banking. Pursuant to this section of the Act, no institution may carry on banking business unless it has a license issued by the Bank of Tanzania.[9]

In making this decision, the central bank should have the ability to screen access to ownership and management to prevent individuals lacking professional qualifications, experience, financial backing and sound ethical standards from obtaining a banking license. In executing the licensing function, the central bank, as required by the law, must scrutinise applicants to determine various key issues before it grants a licence to any applicant. It has to look at the financial soundness of the applicant. This will be evidenced by the bank deposit in any commercial bank in the country in the name of the bank applying for the license. This move will help the central bank to prove the availability of capital for the applicant. Above all these, banks need to contribute some economical benefits to the nation and for this they should therefore indicate their likely contribution to Tanzania's economic development. The likely contribution in this case can, for instance, be measured in terms of employment opportunities to Tanzanians and thereby reducing unemployment.

An applicant's integrity in financial and business dealings is quite important especially for the banking industry due to

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8 See Polizatto (1991)

9 See part II (s.4 through s.11) of the BAFI Act 1991.

the inherent risks involved in banking business. This being the case the Bank of Tanzania has also to be able to determine the integrity of these banks from their past records, if they were in operation somewhere else. Character and experience of the proposed management team is another crucial point to take into account when trying to establish whether or not to grant the license for banking business. Along with all these necessary requirements the central bank must be furnished with details of the intended activities and financial services of the prospective banking firm. They will have, therefore, to submit their feasibility studies, business plans, projections and show how banking skills and expertise of their staff will be developed.

To avoid undue problems that usually arise in many developing economies over the licensed banks, licenses should continue to be granted by those with direct supervisory responsibility and not by any other government agencies. Dale (1982) argues that the decision to grant a license should not be politically motivated and above all it should neither be in a form of patronage nor be designed to serve a special interest group, for example agriculture or housing.

Failure to meet the minimum criteria or to present reasonable projections should result in the denial of a banking license. In most cases, the establishment of specific criteria that must be met reduces the potential for political interference in the licensing process. The ease or difficulty of complying with such criteria can be used as a means of regulating the new entrants into the market. For the licensing authority in the country to assure both Tanzanians and the world at large a stable financial system no criteria for licensing should be skipped.

Prudential Guidelines

The objective of these guidelines is usually to maintain public confidence in banks and financial institutions by ensuring th these bodies lend and invest within tl acceptable and established norms banking, and that their operations regards loans and investments a administered with the highest degree prudence. They thus establish the outsic limits and constraints placed on banks ensure the safety and soundness of tl banking system. They are indeed the ke elements to prevent, limit, or stop tl damage that may be caused by poo management.

According to Polizatto (1990) an Flood (1996) the absence or weakness prudential regulations in certain are takes on critical proportions and coul lead to banking failures and systemi instability. Save for the collapse Meridian BIAO in 1996 and Tanzani Housing Bank (THB) in the followin year, Tanzania have fortunately not ye experienced the so-called systemic failur in its banking history. However, thes facts should not blind the supervisor authority and make them relax fror carrying on its responsibility of ensurin a stable financial system in the country.

Capital Adequacy Regulations

Capital of the bank is necessary to absor unusual losses (See Koehn an Santomero, 1980; Maisel, 1981; an Mutaitina, 1998). In most developin countries, financial institutions ar significantly under-capitalised and i many cases stated capital is negative even before portfolio and other losses ar recognised.[10] The regulatory framewor in these countries often lacks minimun

[10] At one time, as the media reported it, this wa the case with the state-owned banks i Tanzania. NBC was said to b undercapitalized and PBZ with a negativ capital.

capital adequacy guidelines, whether expressed in terms of assets and off - balance sheet items or in relation to risk assets and restrictions on dividend payments when the bank is incurring losses. As a result, capital, as a cushion for unusual losses, is simply not sufficient for the risks that exist both on and off - balance sheet.[11]

Capital adequacy requirements might mitigate the incentives to take on excessive risk[12] and following the suggestions of the Basle Committee in 1988 it is required that the ratio of capital to risk-weighted assets (both on and off-balance sheet), be at least 8 per cent. As soon as a bank fails to meet this requirement, it should re-capitalise or else it should be closed. Dewatripont and Tirole (1993) rationalise such a procedure by building on the literature on the optimal governance structure of firms. The starting point of this literature is that external pressure or interference is a main component of managerial incentive schemes. Since managers dislike interference, interfering after and only after, bad performance provides the best incentives. In the case of a bank, poor performance corresponds with a low capital adequacy ratio, hence, the control model requires intervention in case this ratio drops below a certain threshold. Van Damme (1994) argues that since equity holders have no incentive to intervene in the case of impending insolvency--they want to gamble for resurrection--only the threat of transferring control to the debt-holders can induce bank managers to limit risk. However, since in many developing countries, including Tanzania, depositors are small and numerous, they generally lack the information and power to intervene on an individual basis. Consequently, a regulator such as the central bank is needed to perform their task. Hence, a regulator should not only be in crisis management (i.e. when banks face liquidity problems) but also in the active monitoring of banks even if there is no indication of bank failure. Such active monitoring will presumably also allow the regulator to better distinguish illiquidity problems from insolvency problems.[13]

Lacking adequate capital, the banks' potential for failure is greatly enhanced. Because banks are under-capitalized, management is often forced into hiding losses that would make insolvency apparent. Without appropriate action by bank management, government officials, and bank supervisors, this unhealthy situation may continue until the banks face a liquidity crisis and the government is forced to act. This was the very case for Meridian BIAO and THB whereby the two banks totally collapsed causing significant embarrassments to both the government and the banks' customers. For example, the government was in both cases forced to make the customers accounts good to 100 percent.[14]

In any case, the components of what constitutes capital should be clearly defined.[15] Given that the purpose of capital is to serve as a buffer stock available to absorb unexpected losses, this paper suggests that the measurement of capital adequacy should be related to the areas of greatest risk.

Asset Diversification

Restrictions on geographical expansion or on product diversification often increase the exposure of banks to different types of risks such as credit risk, contagion risks and many others.[16] Banks can increase their returns or reduce their risks or

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[11] See Mutaitina (1998).

[12] See Rochet (1992)

[13] See Boot and Thakor (1993).

[14] See Urassa (1997).

[15] See s.12 of the BAFI Act 1991.

[16] See Inyangete (1996) and Mutaitina (1998).

generally achieve a better combination of risk and return by diversifying their operations (Kaufman, 1996).

Within the same line of executing its supervisory responsibilities, the Bank of Tanzania has issued guidelines on concentration of credit and other exposure limits. Among the objectives of these guidelines is to encourage risk diversification and curtail excessive concentration of risk exposure of any bank or financial institution to one customer or group of customers, industry, economic sector, or activity thereby enhancing the stability of the financial system. These guidelines require banks and financial institutions to make credit available to a broader group of borrowers.

The Supervisory Intensity

A continuing theme in bank supervisory circles is the search for an appropriate supervisory approach (Sheng, 1990). In other words, how a supervisor can best discharge his responsibilities in practice. The two extremes are an off-site supervisory approach and an on-site supervisory approach.

An off-site supervisory approach, which, in its pure form, implies that the supervisor's main function is to undertake an assessment of the soundness of banks based primarily on an analysis of information obtained from completed statutory returns submitted by the institutions being supervised and, to a limited extent, on the information that is publicly available.[17] The major drawback to this approach is that supervisors draw conclusions on information in respect of which they are unable to obtain independent verification, other than the extent to which the information in the statutory returns (some of which are audited by the independent auditors) is corroborated by publicly available information that comes to the supervisors notice. A further drawback is that supervisors' conclusions are based o on the historical information.

Another approach to supervisio the on-site approach. Under this approa the implication is that the total effort the supervisor, with a view to concludi on the soundness of banks, is directed the execution of inspections at t premises of the bank. Such examinatio are usually conducted on a surprise ba (without prior notice to the ba concerned) and at random, on eith selected branches or aspects of t operations of the bank. The examinati could either be a routine inspection or special in-depth investigation to uncov fraud or risk exposure. The focus of su inspections is to obtain and analy original and independent evidence.

Most on-site bank examinatic activities would cover, inter alia, th determination of financial position c bank and quality of operations, includin assets and cash accounts, verification c internal control procedures, thei documentation and compliance. It woul also cover the assessment of managemer quality in order to cover integrity training, and experience level of ban staff; monitor how tightly management i supervised by the board; examine th degree of discretionary powers given t management staff and the way sucl powers are exercised; examine adequacy of staff and staff training; and asses management succession and dual control In carrying out the on-site examinatio the bank examiners must ascertai compliance with laws and procedures a well as testing accuracy of books, accounts, and records thereby verifying that all transactions are properly documented and that all audit trails and authorisations are properly maintained. Other areas of bank examination include verification of assets quality, assessing solvency of the bank and recently the

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17. Pursuant to s.16 of BAFI Act, 1991 and s.47 Bank of Tanzania Act, 1995 all banks and non-bank financial institution are required to submit within a prescribed time their accounts to the central bank.

Table 1: *Supervisory Intensity Matrix*

Level of Assurance Gained From System of Checks And Balances Pertaining to Key Players	*Resultant Approach to Supervision*
No assurance could be gained	Supervisor cannot achieve his mission
Low level of assurance gained	Off-site examination, supplemented by full on-site examination approach
Moderate, but not yet adequate, level of assurance	Off-site examination, supplemented by on-site examination of identified problem areas, as well as high-risk and material areas
Adequate level of assurance (adequate compliance controls and controls over compliance).	Off-site examination supplemented by on-site examination of identified problem areas.

Source: Author's compilation.

detection of the existence of bank fraud, either perpetrated by bank management or shareholders on depositors, and illegal activities such as money laundering.[18] Because of international links in this type of activity, especially when the bank fraud perpetrators tend to siphon funds abroad, there is need for great co-operation among banking supervisors in exchanging information on the *modus operandi* of such fraud and illegal activities and the persons or institutions involved.

However, of the two bank examination approaches, on-site examination is somehow expensive to undertake than off-site one as people will be physically required to visit the banks regardless of the branch network of the banks to be inspected. In this paper, however, it is proposed that the optimal approach should lie somewhere between the two extremes. Since neither approach is a substitute for the other, the important issue is to attain the balance between the two approaches. In other words, a mix of the two approaches would appear to yield the best results. The primary factor determining the optimal mix is the level of assurance to be gained by the supervisor from the system of checks and balances, otherwise known as the system of corporate governance, pertaining to the key players (both banks and non-banks).

As suggested earlier a matrix for supervisory intensity is deemed necessary and the following matrix in table 1, which is self-explanatory, could be useful in this regard.

[18] For a discussion on the effects of money laundering and the economy see Ehrenfeld (1992) and Bosworth and Saltmarsh (1994).

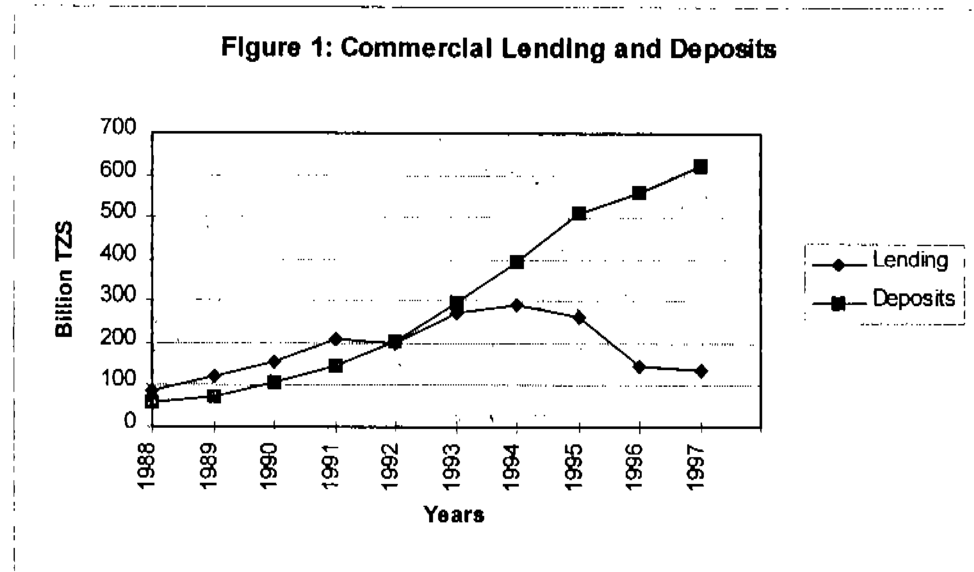
PERFORMANCE AND CONTRIBUTION OF BANKS TO THE ECONOMY

The fact that there exists a strong relationship between financial institutions and economic development is beyond dispute (Nkoba, 1997). According to Kimei, 1987 and Nkoba, 1997 one of the basic features of the process of economic development overtime in a liberalised economy has been the increase in the number and variety of financial institutions and a substantial rise in the proportion of the total of all financial assets relative to gross national product and to tangible wealth. In this section we look first at the performance of the banking system in terms of both deposits mobilisation and allocation of financial resources in the form of loans and other advances. Under the same section the paper looks at the contribution of the sector.

Banks' Performance

The financial infrastructure, particularly the banking sector of a country may offer a positive contribution to the economic development in so far as it is in a position to provide the country with an efficient payment mechanism, encourage and effectively mobilise savings and provide an efficient mechanism of allocating financial resources. Such efficiency is also likely to be reflected in the total and composition of assets of the banks, both at individual level and as a whole (See Tinchy and English, 1993).

Examining the performance entails, therefore, looking essentially at the extent and the efficiency of the banking system in accomplishing the above mentioned tasks.



Source: Bank of Tanzania (1997)

Deposits Mobilisation

The mobilisation of savings is an important process that may assist a country to foster its economic development. How individuals and institutions can save very much depends upon their wealth holdings and in particular on their current incomes. Through savings, financial resources are accumulated thus making the financing of investments possible. How efficient and effective the banking sector in Tanzania has been in mobilising deposits can be viewed in two ways. One is to assess the respective contribution of the economic sectors to total bank deposits and of course the trend in deposit taking by banks.

For the purpose of proper analysis of the banks' performance the paper considers, in the same figure, the trend and relationship that exists between lending and deposits. Nevertheless, a detailed discussion of banks' performance in terms of lending will be provided under separate sub-section. Regarding deposits mobilisation by the banking sector in the period covered by figure 1, banks performed fairly well in the sense that there was a remarkable increase through out the period under review. While less than a hundred billion shillings was mobilised in the year 1988, the figure increased by more than six times in 1997 to T.Shs. 623 billion. Considering the changes that followed the enactment of the Banking and Financial Institution Act, 1991 it is pertinent for one to say that a percentage increase of about 320% could be associated with the relative increase in the number of banks from two in early 90s to the current twenty banks in the country.

The composition of these various deposits is spread into four categories namely: demand deposits, time deposits, savings deposits, and foreign currency deposits. There is uneven distribution of these deposits between those deposits that earn customers some interest and those that do not earn them any interest. Almost all the banks in the country pay a modest amount of interest in savings accounts, time deposit accounts, and to foreign currency accounts; but for a certain specified amount and types of the currency in question. Table 2 shows a consistent characteristic, although uneven, of increases in deposits through out the period under review.

Table 2: *Level of Deposits in Banks for the Period 1988-1997*

End of Year period	*Demand Deposits*	*Time Deposits*	*Savings Deposits*	*Foreign Currency Deposits*	*T.Shs. m. TOTAL*
1988	33698.7	14504.7	9433.1	470.4	58106.9
1989	41323.9	20794.4	11593.6	1488.5	75200.4
1990	53165.8	35002.6	17065.9	3521.4	108755.7
1991	72321.2	43,383.5	26508.5	5,761.2	147974.4
1992	90421.7	62,459.1	36633	16,957.6	206471.4
1993	124924.4	69,607.5	50396.2	53,540.8	298468.9
1994	153316.5	84,799.5	72064.9	83,254.0	393434.9

1995	183971.4	91,210.2	94199.9	139,216.3	508597.8
1996	191550.5	122436.6	113340.7	133,072.4	560400.2
1997	215706.2	129668.8	130915	146,757.5	623047.5

Source: Bank of Tanzania (1997)

Using table 2, the paper discusses, albeit briefly, the general behaviour of the savers in the period 1988-1997. It shows that a larger portion of the deposits is mobilised from the demand deposits type. The reason for this could only be associated with the convenience availed to a customer when he or she requires making some withdrawals. As the name suggests and unlike other types of deposits, demand deposit (or current account) whether in local or foreign currency requires no prior notice of withdrawal to be served by the customers to their bankers. The table shows for example that in 1991 a total of T.Shs. 69,892 million or 47.2% was mobilised by banks as both time and savings deposits. In the same year a total of T.Shs. 78,082.4 million or 52.8% of the total deposits was in terms of non-interest bearing accounts i.e. demand deposits and foreign currency deposits.

The trend continues in the same direction throughout the surveyed period. In 1997 banks were able to mobilise total financial resources amounting to T.Shs. 623,047.5 million. Of this amount T.Shs. 260,583.8 million or 41.8% was in various savings and time deposits. It is no doubt that this still obeys the same characteristics as pointed out earlier regarding the preference of banks' customers towards the interest bearing and non-interest bearing type of accounts. Perhaps it is for this reason that T.Shs. 362,463.9 million or 58.2% was available in the non-interest bearing accounts.

Generally, the percentage growth in total deposits was increasing significantly. It was 29.4%, 44.6%, 36.1%, 39.5%, 44.6%, 31.8%, 29.3%, 10.2%, and 11.2% in 1989, 1990, 1991, 1992, 1993, 1994, 1995, 1996, and 1997 respectively. This trend needs to be considered satisfactory by the banking sector and as the paper argued earlier such a performance has something to do with liberalisation of the banking sector.

Lending and Holdings of Securities

Lending is another aspect that indicates the performance of the banking system. It shows the way by which financial resources are allocated by banks into various sectors of the economy. Such allocation is done in principle through credit extension to these various economic sectors. As indicated earlier in figure 2, the trend in lending by banks has not been impressive for the period 1988-1997.[19] With the exception of 1994, there was no single year in which lending went as far as T.Shs. 200 billion (see figure 1).

The reason for this downward spiral in direct lending by banks could be due to government monetary paper (i.e. treasury bills and government bonds) gaining popularity. The rate of customers' defaults and direct abuse of the lending facilities is considered to be high causing banks to be sceptical as to whether or not the money so lent will ultimately be repaid. There are no readily available data to justify this

[19] It should be noted that the term "lending' comprises of all facilities extended to various customers as loans. overdrafts. and commercial bills (both local and foreign).

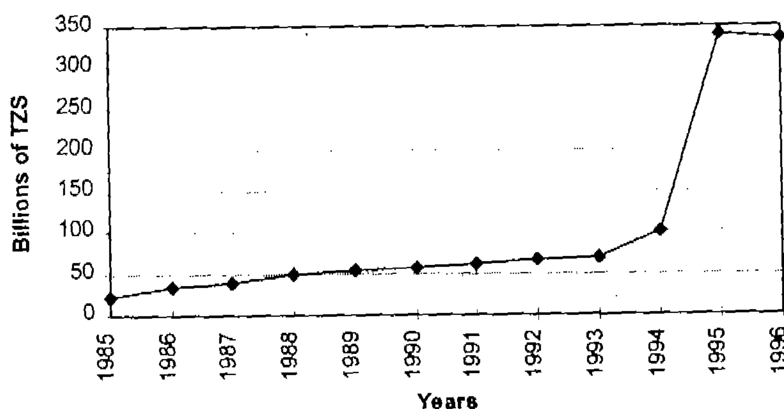
assertion, but the sharp rise in demand for investment in securities as shown in figure 2 may give some clue on the matter.

There has been a modest rise in the volume of securities that were held by different types of customers for the decade ending 1994. But a sharp change appears to have occurred in the demand of securities. As pointed out earlier, this was due to a large group of banks starting to get doubtful over the likelihood of customers to default and as a result government outstanding stocks, bonds and notes recorded an unprecedented rise in volume from T.Shs. 100 billion to T.Shs. 350 billion or 250% in the period 1994-1997.

CONTRIBUTION OF BANKS TO THE ECONOMY

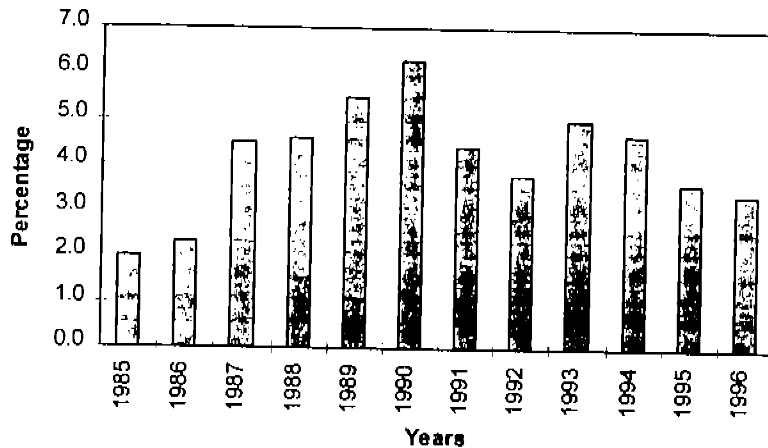
Banks offer various services to their customers; which in turn contributes to the economic development of the country. The services may vary between one bank and another depending on the size of the bank and probably the market share such bank enjoys in the respective country. However,
this paper discusses those services that seem to be commonly offered by any bank. These services at different levels among the banks may include the following: expanding the money supply through making of loans and investments; providing an outlet for the savings of business, households, and government units; as well as offering a means of payment for purchases of goods and services. Other services include providing fiduciary (trust) services to their customers; supply of international financial services; and providing investment banking services which involves advising major corporations and other businesses on their financing needs and merger programs.

Figure 2: Government Outstanding Stocks, Bonds and Notes by Holders



Source: Bank of Tanzania (1997)

Keeping in mind the three approaches used in measuring any country's wealth (th income approach, the expenditure approach, and the output approach) then one should agre with Lipscombe (1993) that banks, to a certain extent do contribute to economi development as shown in figure 3 which is self explanatory. Directly the banks pay salarie



Source: Bank of Tanzania (1997)

to their employees, and they earn profits that are added to all the other incomes in the income method of calculating GDP. On the expenditure side, their purchases of capital good such as furniture are very large. Under the output measure, all the banks' products and services contribute to GDP. Indirectly the banks facilitate the payment of all incomes used in income measure of GDP. On the expenditure side, as discussed earlier, banks help consumers buy the nation's output by giving a wide range of lending products.

CONCLUDING REMARKS

This paper has analysed the banking sector in Tanzania and the impact of liberalisation of the banking industry to the economy. It has argued for the positive part of the liberalisation process. For example the number of projects that were approved, and the number of people who were able to get employment has been shown. We have emphasised the need for the regulatory authority not to relax the criteria for entry and suggested that the authority must keep its eyes open to ensure smooth and stable banking system.

The paper has also discussed the supervisory intensity for banks in the country and we have proposed a working matrix that might ensure a system of corporate governance. Within the same framework the paper has suggested that since the two extremes of bank supervision i.e. on-site and off-site examination, are not a substitute to one another, then it is important to attain the balance between the two approaches. It is argued that a mix of the two approaches could save that purpose.

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