www.repoa.or.tz

PB 8/2020 Dec. 2020

REPOA Knowledge is Power

Repoa Brief

The effects of institutional bottlenecks on enterprise development and competitiveness in productive sectors in Tanzania

By Cornel Jahari

Key messages

- Despite gradual improvements in enterprise development and competitiveness, Tanzania still lags behind her East Africa regional compatriots
- Large enterprises are more affected by existing bottlenecks to competitiveness than Micro, Small, and Medium Enterprises
- Institutional collaboration remains key to resolving some of these bottlenecks, thus enhancing enterprise development and competitiveness

Introduction

Tanzania has sustained relatively high economic growth over the last decade, averaging 6-7% a year. Until 2017, the economy grew at an average of over 7% a year. This economic growth rate has generated some gains in poverty reduction and coincided with changes in the structure of the economy. According to the Household Budget Survey (HBS), basic needs poverty declined from 28.2 per cent in 2011/12 to 26.4 per cent in 2017/18. Similarly, food poverty dropped from 9.7 per cent in 2011/12 to 8.0 per cent in 2017/18. Changes are also observed at macro levels, which includes structural change and some productivity improvements (Diao, Kweka, & McMillan, 2018). The share of agriculture to GDP has declined over time while the share of industry and trade has increased (URT, 2019). There has also been a markable shift in the structure of exports, as the share of traditional exports in total goods exports declined from 40% in 2000 to 16.2% in 2018, with an increased observed for non-traditional exports, including minerals, manufactured goods, and tourism receipts. Investment growth has remained positive, but this might be difficult to sustain FDI inflows appears to decline, and private sector credit growth remains on the low side.

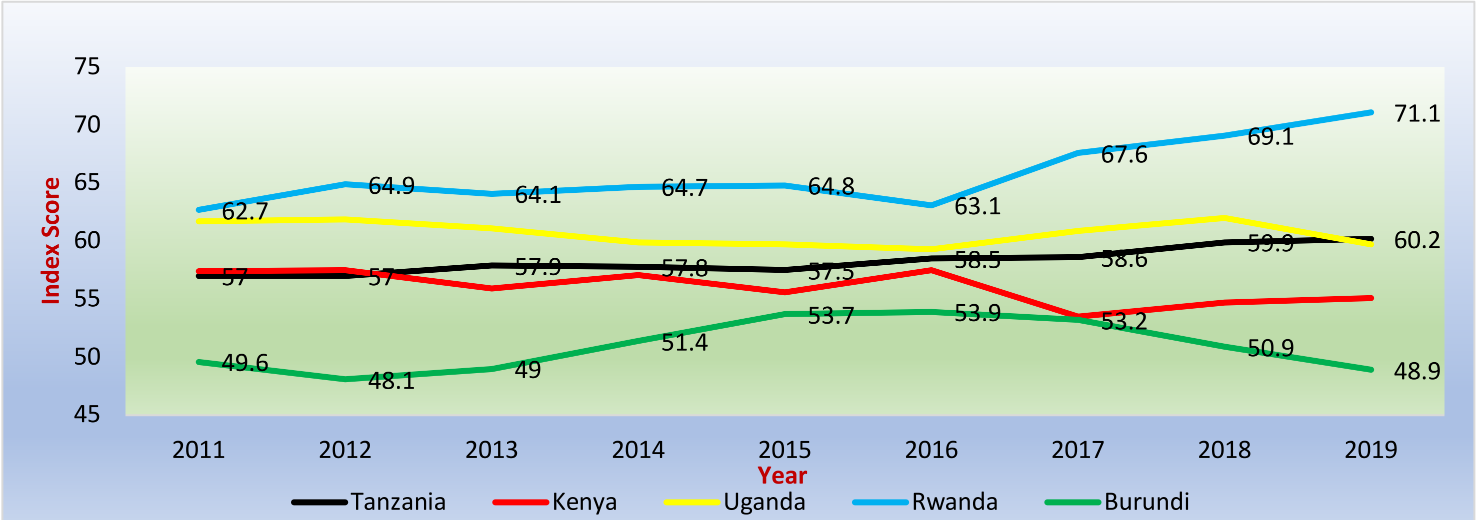
Tanzania has implemented many reforms to its business environment in response to changes to its economic outlook and global competitiveness rankings (Schwab, 2019). These include increased investments in infrastructure at reducing infrastructure gap, some interventions to institutional level constraints including over-regulation, institutional instability, weak coordination, and regulatory side disincentives created by cumbersome taxation and escalating tariff structure. However, the implementation of these soft sides of the reforms appears to be slow, as some investors and the business community continues to raise concerns. Seemingly inadequate understanding and knowledge about the constraints necessary for designing an appropriate remedy could contribute to limit the effectiveness of Tanzania's business environment reforms.

This policy brief flags areas of crucial policy concerns in the context of the prevailing legal and regulatory framework for enterprise development and competitiveness. It draws on analyses and findings from REPOA's Research Project on Institutional Analysis of Enterprise Development and Competitiveness (EDC) in Tanzania. The research draws on analyses of primary and secondary data from the World Bank's Country Policy and Institutional Assessment (CPIA) indicators, World Development Indicators (WDI), World Bank Enterprise Surveys (WBES) and the Annual Survey of Industrial Production data (ASIP).

Findings

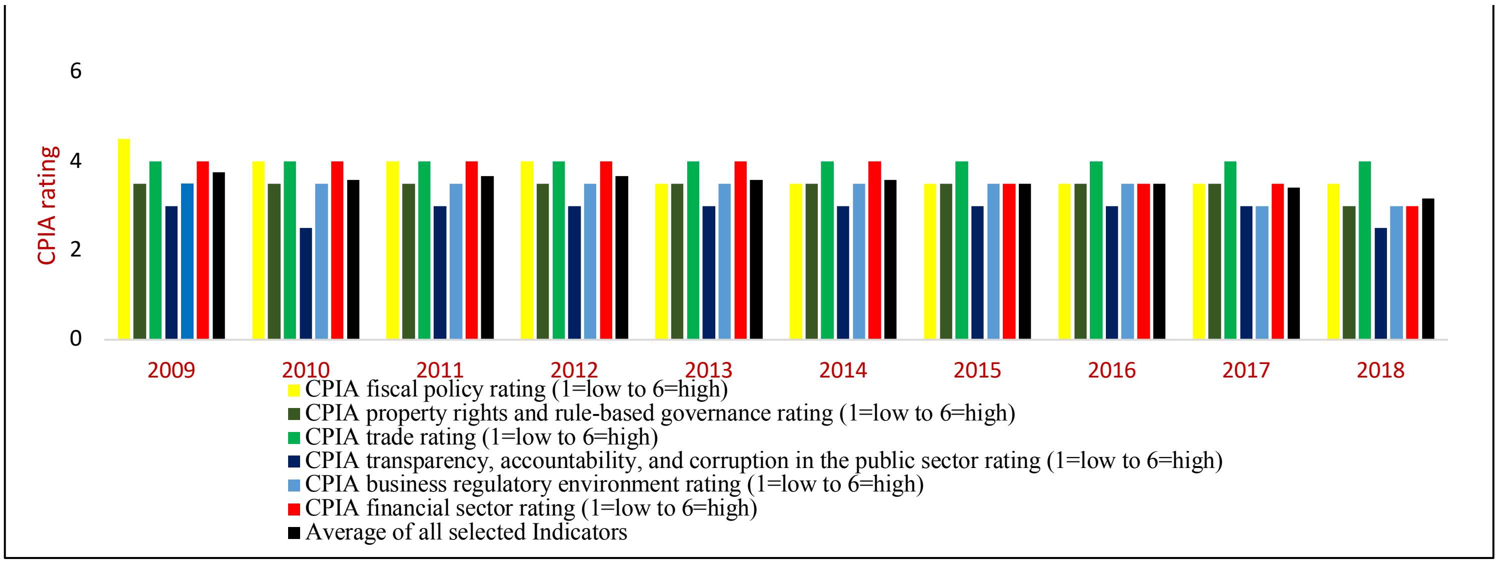
Tanzania is improving on economic freedom indicators, although it still lags in other indicators. With the use of four sets of Economic Freedom Indicators (Rule of Law, Limited Government, Regulatory Efficiency, and Open Markets) as measured on a scale from 0 to 100, Tanzania has shown slight score improvement between 2011 and 2019 above that of Kenya and Burundi, getting at par with Uganda, and only below Rwanda. (Figure 1)

Figure 1: Annual Index of Economic Freedom for selected Countries



Performance of Institutional Quality

The Country Policy and Institutional Assessment (CPIA) for selected indicators including (Fiscal policy, property rights and rules, trade, transparency-accountability and corruption in the public sector as well as the business regulatory environment) is used to measure the quality of the institution in EAC. Tanzania's performance in the quality of institutions over the 2009-2018 period compared with other EAC countries shows that none of the indicators showed significant improvement. Indeed, only trade rating indicator had the same score for all ten years (a score of 4), while the remaining indicators declined over time. Overall, the selected CPIA indicators show that institutional quality in Tanzania has been gradually declining (Figure 2).

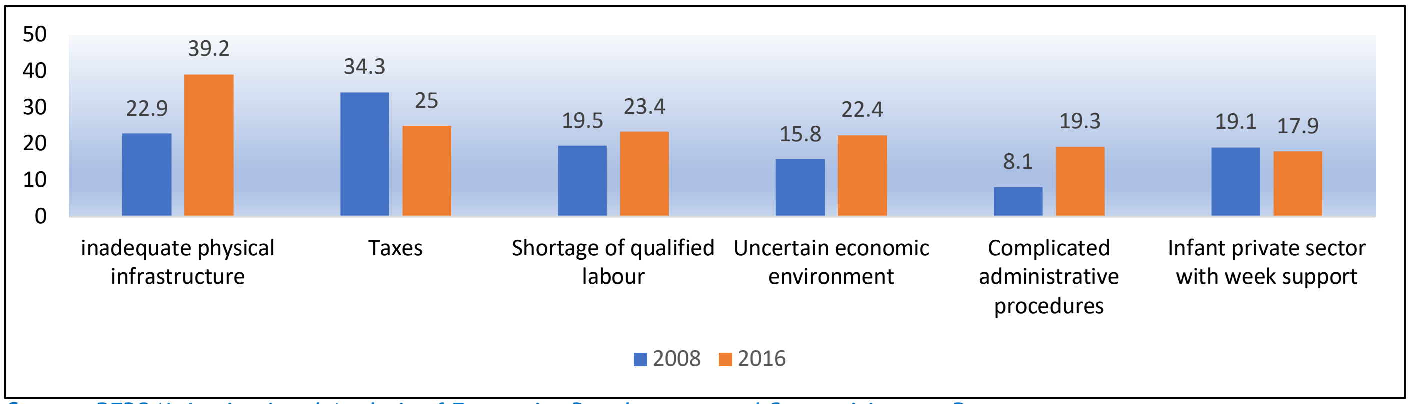


Source: REPOA's Institutional Analysis of Enterprise Development and Competitiveness Report

The challenges of Institutional Factors in Promoting EDC in Tanzania context

Analysis of firm-level survey data shows that institutional challenges have persisted, though changing over time. The results show that in 2016 inadequate physical infrastructure (roads, electricity, water etc.) was identified as the most binding constraint by the highest number of firms (39.2%), followed by taxes (25%), shortage of qualified labour (23.4%), and lastly, infant private sector with weak support (17.9%). Moreover, only taxes and infant private sector with weak support challenges seem to have reduced between 2008 and 2016 as reflected by a decreasing percentage number of firms that identified them as institutional challenges (from 34.3% to 25% for taxes and from 19.1% to 17.9% for infant private sector with weak support). (see figure 3).

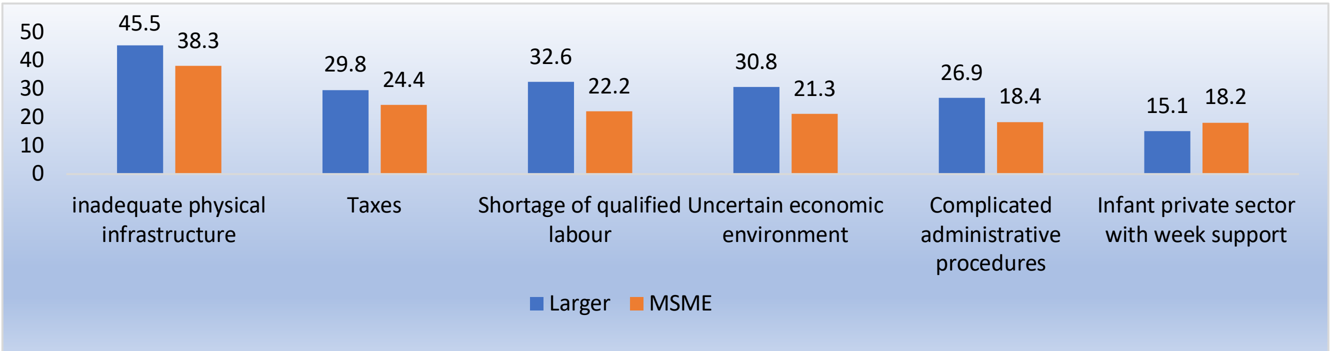
Figure 3: Proportion of firms identifying Institutional challenges in 2008 and 2016



Source: *REPOA's Institutional Analysis of Enterprise Development and Competitiveness Report*

By distinguishing frequencies of the challenges by the size of firms, majority of both large (45%) and Micro, Small, and Medium Enterprises (MSMEs) (38.3%) identified inadequate physical infrastructure as a significant challenge for their businesses. However, large firms are more affected by physical infrastructure, labour, uncertain economic environment, complex administrative procedures, and taxes than MSMEs except for the infant private sector with weak support (see figure 4).

Figure 4: Proportion of firms identifying institutional challenges 2016



Source: *REPOA's Institutional Analysis of Enterprise Development and Competitiveness Report*

The prevalence of institutional challenges for firms

Despite the existence of institutions supporting the development of firms, there is a general lack of awareness of their presence and functions among firms. According to the ASIP data, 41% of establishments were not aware of the various functions or services offered by associations which could be among the reasons why there are few firms registered to associations. Indeed, over two-thirds of firms which did not co-operate or receive technology or production services from Public Technology Intermediaries cited lack of awareness of the institutions or services offered. Nonetheless, data shows that some of the institutional challenges are more prevalent by firm size and ownership characteristics. Majority of firms are challenged by uncertainty in the economic environment; infant private sector and complicated administrative procedures; and that these challenges appear to be significantly more severe for private than for public sector firms (see table 1).

Table 1: Prevalence of Institutional Challenges across different Firm Characteristics in 2016 (% of firms)

Firm Characteristics	Uncertain economic environment	Infant Private Sector with weak support	Complicated administrative procedures
Small	74.05	83.86	75.21
Medium	10.34	6.59	9.03
Large	15.61	9.55	15.76
Total	**100**	**100**	**100**
Public	6.35	4.55	6.72
Private	92.2	94.32	92.44
Mixed	1.45	1.14	0.84
Total	**100**	**100**	**100**

Source: REPOA's Institutional Analysis of Enterprise Development and Competitiveness Report

References

Adesina, A., Kim, J. Y., & Schwab, K. (2017). *The Africa Competitiveness Report 2017, Geneva: WFF*.

Conclusion and Recommendation

While the ongoing Blueprint initiative to improve the business environment as the country striving towards industrialization economy is in place. A strong government commitment and political will are required if Tanzania is to further enhance enterprise development and competitiveness.

Hence, the following policy recommendations to improve enterprise development and competitiveness are suggested:

First, to address inadequate physical infrastructure, the government should revisit access to key services such as water connection, availability of building permit if the country is to be to be competitive in the region given huge government investment on railways, roads, electricity currently under implementation

Second, to resolve taxation challenges, the government should develop a core set of indicators that would support meaningful monitoring and assessment of capacity improvement in tax administration in areas of efficiency, tax dispute resolution, accountability, transparency, the integrity of the taxpayer base, assessment of risk and supporting voluntary compliance over time.

Third, In a context of dynamic and complex labour markets, to improve the availability of qualified labour, the government should work more proactively with companies and industries gathering intelligence on current and future skills needs to support better matching of training and jobs and link technical and vocational training with general education and higher education.

Fourth, to reduce uncertainty about the economic environment, the government should facilitate the inclusion of the private sector's perspective in stabilizing macroeconomic and microeconomic factors that influence business decisions in the entire economy

Fifth, to simplify administrative procedures, the government should diminish administrative misconduct by practicing transparent regulations, and legal efficiency framework and simple rules and procedures for accessibility, convenience, timeliness, low cost, and fairness in starting a business, dealing with licenses, registering property, paying taxes, enforcing contracts, hiring and firing workers, getting credit, protecting investors, trading across borders, and closing a business

Sixth, to help the infant private sector, the government needs to formulate fiscal policies that deliberately facilitate infant private sector access to financial resources through (credit, guarantees, investment funds and foreign investment), to knowledge (training and dissemination and exchange of technologies), as well as to market contacts (linkages and business promotion activities).

References

Aikaeli, J. (2012). *Improving competitiveness for SMEs to harness available trade and investment opportunities: The case of Tanzania*. Huria: Journal of the Open University of Tanzania, 11(1), pp.25-43.

Ball, J. (2015). *Why is enterprise seen as so important in economic development? Retrieved from IWA: https://www.iwa.wales/click/2015/02/why-is-enterprise-seen-as-so-important-in-economic-development/*.

Diao, X., Kweka, J., & McMillan, M. S. (2018). *Small firms, structural change and labor productivity growth in Africa: Evidence from Tanzania*. World Development 105 (May): 400-415. .

Holliday, S. (2019). *Entrepreneur. Retrieved from Entrepreneurship Is the New Engine of Global Collaboration*. https://www.entrepreneur.com/article/325800.

Schwab, K. (2019). *The Global Competitiveness Report*. Cologny/Geneva: World Economic Forum.

Snodgrass, D., & Winkler, J. (2004). *Enterprise growth initiatives: Strategic directions and options. Development Alternatives Inc.*

URT. (2019). *The Economi Survey*. Dodoma: Ministry of Finance and Planning: The United Republic of Tanzania.

WB. (2019). *Tanzania Economic Update: Human Capital, The Real Wealth of Nations* . World Bank .

REPOA Resource Centre

Opens from Tuesday to Friday from 10:00 am to 1:00 pm, 2:00 Pm to 5:00 pm. Online library is open 24 hours

REPOA

157 Mgombani/REPOA Streets, Regent Estate, P.O. Box 33223, Dar es Salaam, Tanzania

Tel: +255 22 2700083 Cell: +255 75 409 1677 Fax +255 22 2705738

Website: www.repoa.or.tz Email: repoa@repoa.or.tz