Tanzania's Growth Experience Following Economic Reforms: Comparative Perspectives with Vietnam

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Abstract

Tanzania and Vietnam followed socialism ideology for decades, but both countries embarked on market reforms in the 1980s. This paper traces the major trends in economic transformation of Tanzania following reforms, and compares with the Vietnam experience with specific focus on agriculture and industry. It is demonstrated that socialism failed to generate the anticipated economic development mainly due to weaknesses in the instruments used to implement the ideology. The parastatal corporations became inefficient and could not produce enough goods to meet demand. While Tanzania approached economic reforms by abandoning agriculture in favour of private sector-led industrialization, Vietnam's priority was on integrating the public and private sectors into an overall system. As a result the two countries have followed different economic trajectories with Vietnam performing far better than Tanzania. The paper recommends learning from history and from diverse experiences to guide Tanzania's growth diagnostic work and strategies for scaling up growth.

Key Words: Tanzania, Vietnam, Economic liberalisation, Agriculture, Industrialization, Socialism

1. Introduction

The history and experiences of both Tanzania and Vietnam regarding their economic policies is fundamentally characterized by a mixture of complex trends. While Vietnam went through a violent and prolonged war that created the need and urge for reconstruction, Tanzania was paralyzed for so long that it is ready to leapfrog the development process if it can. The two countries have been managed on centralized bureaucratic lines for decades, but both countries have now embarked on market reforms, and the timing of these reforms in Vietnam and Tanzania was quite close.

Tanzania began to discuss reforms and made the first moves in the early 1980's. It adopted an economic reform program in 1986 after experiencing a steady decline in economic growth in the late 1970s that led to a financial crisis in the early 1980s. The crisis was partly a result of economic policies pursued by the country under a public sector–led economy embedded in the 1967 Arusha Declaration, and partly a result of exogenous factors, including deterioration in the terms of trade in the late 1970s and early 1980s, the collapse of the East African Community in 1977, and the war with Uganda during 1978–79.

Vietnam's gross domestic product (GDP) per capita in 1985 was US$130 per year, making it one of the world's five poorest countries (World Bank, 2004). The country made first tentative steps towards reforms in the mid-1980's, and began vigorous implementation of new policies from 1989 onwards. At the start of the 1980s, Vietnam had a command-controlled economy directed by the state. The *Doi Moi* reforms were stimulated by the recognition of Vietnam's severe economic problems of the 1980s, and the need to restructure the economic system to address these problems (Turley and Selden 1992; and Ha Huy Thanh 2000).

The purpose of this paper is two-fold. First, it traces the major trends in the economic transformation of Tanzania following reforms, and compares with the Vietnam's experience. Two sectors; agriculture and industry are given specific focus. Secondly, an attempt is made to explore the lessons that the experience of Vietnam provides to inform the growth strategies in Tanzania.

2. Tanzania and Vietnam at the Beginning of the Reform Process

At the beginning of the reform process, the two economies had some similarities. In terms of policy orientation, both countries had, in principle, a high degree of government economic control before initiating reforms. While Vietnam was more populous (with more than twice the population of Tanzania), its GDP per capita was at a similar level to that of Tanzania at the end of the 1980's (Figure 1).

3. Comparing Reform Outcomes

Tanzania's reform process has been gradual and at best cautious but steady. The changes in the economic policy regime led to increased levels of economic activity stemming from liberalization efforts, availability of consumer goods, and market determined producer prices. Economic performance improved, albeit gradually. GDP growth averaged about 4 percent per year between 1987 and 1992, reversing the real per capita income decline experienced in the early 1980s. Official Development Assistance (ODA) rose sharply to US$1.08 billion in 1991 from US$666 million in 1986, reflecting resumption of donor inflows in support of economic reforms. Although the rate of inflation declined slightly, it remained high (above 30 percent), fueled mainly by growth in domestic credit reflecting lending to loss-making agricultural marketing boards and cooperative unions, which continued to exert influence. As a result of the temporary setback in macroeconomic policy during the first half of the 1990s, GDP growth averaged less than 2 percent per year between 1991 and 1995, reversing real per capita GDP growth attained during the preceding six years. Meanwhile, gains made earlier in reducing inflation were reversed: inflation rose from about 22 percent in 1992 to 37 percent in 1994.

Macroeconomic stability was achieved in the late 1990s. Inflation was reduced from about 30 percent in the 1980s and early 1990s to single digits in late1990s, when severe fiscal imbalances were brought under control through prudent fiscal management; inflation in 2006 was 7.3 percent. Acceleration of structural and institutional reforms, as well as creation of new institutions, led to improvement in the investment climate, and increased Foreign Direct Investment (FDI) flows. Government revenue, excluding grants, improved from about 11.8 percent of GDP in 1993 to 13.5 percent of GDP in 1996. However, the revenue ratio to GDP declined to 12 percent in 1999. It has since stabilized around 13 percent. The overall deficit excluding grants improved from 7.5 percent of GDP to 2.8 over the same period. During this period, GDP growth rate reached 6.2 percent in 2002, up from 3.6 percent in 1995, and growth in per capita GDP accelerated to 4.2 percent in 2002. The balance of payments improved significantly, largely because of the resumption of large donor inflows and export earnings: particularly from nontraditional exports such as gold, gemstones, and fish products. Overall gross foreign reserves rose from the equivalent of 1.6 months of imports at the end of December 1995 to more than 6 months of imports at the end of December 2002.

Tanzania's sustained commitment to economic reforms triggered its eligibility for debt relief under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative in April 2000, making it one of the first countries to reach the completion point and to benefit from irrevocable and substantial debt reduction. Debt reduction in turn paved the way for additional donor inflows. The additional resources, including from the HIPC debt reduction, allowed the government to increase budgetary expenditure allocations to social sectors which led to visible improvements in public service delivery, in particular education and health.

The more recent trends in key macroeconomic indicators provide a mixed picture. Inflation rates, fiscal deficits, and the trade balance have shown signs of slippage since 2002/03. In addition, while there has been an increase in credit to the private sector, it remains limited to a small number of firms, and a large portion of bank liquidity is invested in government securities. The spread between lending and savings rates continue to be high, reflecting a continuation of high cost of borrowing from commercial banks, and low incentives for those savings. There has been a slowdown in FDIs, most of which remain heavily concentrated in the natural resource sector with minimum spillovers to other parts of the economy.

Although the Tanzanian economy has responded positively to reforms, and the country is currently seen as one of the more successful reforming African economies, performance in terms of growth – both the level of growth and acceleration compared with earlier years of crisis has been less dramatic than in the case of Vietnam. All the indicators suggest that Vietnam has been significantly more successful than Tanzania (Figure 2).

During the 1990's Vietnam enjoyed a very high growth rate both in comparison to developing countries at a similar income level and to other transitional economies (with the exception of China).Vietnam also experienced very high rates of export growth based on fast output growth in agriculture and industry (Van Arkadie and Do Duc Dinh, 2004). The considerably transformed structure of a number of industries led to the development of certain key products. A number of industrial and export processing zones with many production establishments using modern technologies were established. Along with the development of large-scale industrial establishments, the government attached great importance to the development of small and medium-sized enterprises with a view to creating more employment and raising incomes (The Socialist Republic of Vietnam, 2003). Tanzania on the other hand has not achieved the buoyant and diversified export growth of the kind that has powered the Vietnamese performance.

Deep changes in Vietnam's economic system were implemented without a decline in economic activity, the economy growing despite the sudden collapse of Soviet aid, the U.S. boycott and the absence of financial assistance from the multilateral aid institutions before 1993. Gross Domestic Product (GDP) per capita was $206 US in 1990, increasing to $423 US in 2004. In terms of purchasing price parity (PPP) measures, Vietnam's GDP per capita was approximately $2500 in 2003, which represents a major advance in living conditions. From the early 1990s to 2005, poverty declined from about 50 percent to 29 percent of the population. However, progress varied geographically, with most prosperity concentrated in urban areas, particularly in and around Ho Chi Minh City. In general, rural areas also made progress, as rural households living in poverty declined from 66 percent of the total in 1993 to 36 percent in 2002. By contrast, concentrations of poverty remained in certain rural areas, particularly the northwest, north-central coast, and central highlands.

4. Sectoral Growth and Structural Transformation

The modern concept of transformation recognizes that with development in country economies, the share of the agricultural sector will shrink, leaving space for expansion of the industrial and service sectors. Indeed as economic development takes place the importance of agriculture drops. This has been well described by Kuznets (1966) and Chenery and Taylor (1968) in their classical works on the evolving structure of economies. In Vietnam, though the agricultural sector was growing rapidly, its share in GDP dropped nearly a half from 40.2% in 1986 to 23.6% in 2002, leaving space for the share of industry to expand from 27.4% to 38.3% and services from 32.4% to 40% in the same years. These facts illustrate a high rate of structural shift towards industry in Vietnam, and also that this shift in shares is supported by growth of the agricultural sector.

Tanzania's agriculture contribution to GDP has also dropped (although slightly less than Vietnam) from around 30% in the late 1990s to about 28% in 2005. Non-manufacturing and non agro-based industries, (i.e. construction, and mining) have increased their contribution to GDP. Growths in these sectors, however, have had minimal welfare benefits, as their value chains are yet to augur into the nascent domestic processing and service systems. Contribution of the service sector has increased significantly.

5. Performance of the Agricultural Sectors

In Tanzania, stated policies that guided government activity in the agricultural sector can be summarized as follows: reversing price distortions and recuperating losses due to inefficient (state-run) processing and marketing industries; using the market rate of exchange for agricultural exports; revitalizing export-processing industries through divestiture and encouragement of private sector participation; and continued reduction of state participation and control in produce marketing and input supply. Other, more generalized policy intentions stated but which have never yet been fully implemented on the ground were to (i) improve the Government's ability to design and implement market based incentives for agricultural production, processing and inputs supply; (ii) improve the functioning of markets for all factors of production, (iii) induce technological change by improving the efficiency of input supply markets and by increasing the effectiveness of Government's agricultural extension and research services.

Overall sector performance in Tanzania during the post-reform period 1985-2005 was respectable but not outstanding. Agricultural GDP grew by 3.5 percent per year over 1985-90; 3.3 percent over 1990-1998, and 4 percent over 1998-2005. In the early period, food crop production grew quickly in response to domestic market liberalization, while export production was stagnant. By 1990, the increased food availability had eliminated the need for food imports.

However, weak marketing and poor distribution chain hindered an increase in food supplies in urban areas (Mwase and Ndulu, 2008). The non-traditional agricultural export sector increased five-fold between 1985 and 1991 (Mans 1994). Since 1990, food crop production growth slowed to approximately the rate of population growth, while export crops posted an impressive 7.7 percent rate of growth. Export liberalization and exchange rate depreciation improved the incentives for export crop production, and Tanzanian farmers responded well in spite of continuing institutional and credit problems in the sector.

Vietnam is a largely agrarian society, with two-thirds of the labor force working in agriculture, forestry, and fisheries (FAO 2005). In Vietnam, reforms in agriculture and rural areas helped to increase rapidly agricultural output. Per capita food production was boosted from 303 kg in 1990 to 444 kg in 2000, and revenues from agricultural exports more than quadrupled from US$ 1 billion in 1990 to US$ 4.3 billion in 2000. Agricultural growth rates increased from an average of 1.8% between 1985 and 1988, to 3.9% between 1988 and 1994, and 4.4% between 1994 and 2000.

Although rice, the country's single most important crop, has always played an important role in the Vietnamese economy, the economic reforms shifted agricultural production away from subsistence towards cash cropping. As a consequence, Vietnam has gone from being a rice importer in the 1980s to the world's second largest rice exporter, after Thailand. Rice production increased by about 1 million tonnes of rice each year, turning it from a food-deficient country and importer of around 0.5 -1 million tonnes a year in the pre-reform period to be an exporter of 3 -3.5 million tonnes of rice a year. It has also become a large exporter of coffee, rubber, cashew nut, tea, pepper, and fish-farming products, as well as developing a range of products for the domestic market, such as maize, cotton, soy bean, sugar cane and dairy, thus allowing the country to save hard currency that would have been needed for food imports.

6. Performance of the Industrial Sector

In Tanzania, the performance of the industrial sector in the pre-reform period was characterized by gross inefficiencies, low (and sometimes negative) output growth, low capacity utilization, low productivity and poor export performance (Shitundu and Mjema, 1995). That performance was mainly attributed by internal factors (i.e. the highly regulated environment (in terms of policies and institutions) in which the sector was operating, as well as external factors. Tanzania's industrial output showed relatively low growth rates in the early years of reforms (1990s) but has shown large increases in recent years. In Vietnam, statistics reveal high growth rates in the industrial sector at the time when the *Doi Moi* policies were adopted, and increased at a lively rate throughout the reform period. However, it seems that manufacturing industry performed better than mining and construction. The difference is explained below.

6.1.1. Human Capital Development

One area in which Viet Nam had a clear lead over Tanzania in the pre and post -reform period was in relation to investment in human capital. There was a good deal of effort in technical and professional training, that involved active utilization of opportunities for technical training abroad, as well as development of national technical training capacity. This had begun even in the early stages of independence struggle. A strong commitment to investment in human capital in Vietnam included a comprehensive basic education program, resulting in very high levels of literacy in rural as well as urban areas. Adult literacy rates were at 87.6% in 1989 and had reached 90% in 1999, while for Tanzania, they were at 59% in 1988 and only reached 69% in 2002 (UNESCO- Institute of Statistics, 2008). By 1999, while the population of Vietnam was only slightly more than double that of Tanzania, secondary school enrolment in the latter country was only about 4 percent that of the former, and tertiary enrolment about 2 percent. Comparison in enrolment figures for the key disciplines at tertiary level also reveals a striking difference.

Competitive advantage is based on continuing efforts, at the level of the firm and the economy, to enhance capabilities to add value to basic resources and commodities, penetrating new and more profitable markets. Higher value added processes tend to require higher levels of education. In management and technical education, this is a matter of skills and knowledge pertaining to day to day operation of a business, design and set-up of production processes, and world markets which are gained partly from formal education; but even more from learning-by-doing.

Vietnam was successful in developing and utilizing a robust capability in intermediate technology, constructing buildings and other physical facilities and producing goods for the domestic market cheaply and of appropriate standard for a low income market, while more recently beginning to adapt its technology to the more demanding standards required for export markets. Investment in human capital paid off in terms of the receptivity to technical change and the economic opportunities emerging in the reform period. By comparison, Tanzania's economy at the inception of reforms did not have a sound base of adequately qualified and trained work force that is essential for rapid economic growth and effective diversification of its production and export bases.

6.1.2. Agricultural Sector Initiatives

In Tanzania, generally reforms in the agricultural sector opened up markets by formally allowing private traders to invest in marketing and processing. However, there haven't been efficient operations within the liberalized markets. Many problems cited in different studies indicate gross inefficiency in the production and marketing systems such that most of the farmers have not captured the full potential benefits of their production regimes despite operating under a liberalized market scenario (see Cooksey, 2002; Kashuliza and Mbiha 1995; Meertens, 2000; Rweyemamu 2002).

The withdrawal of the state from Tanzanian agriculture left a void particularly in rural areas. This can be seen as a transitional problem in moving to a market-oriented system, but after two decades, the growth of the institutional and legal environment necessary to nurture the growth of economic transactions under market principles has been slow. There is a clear need for faster progress in creating a reliable and enforceable regulatory environment for internal and external agricultural trade, including measures and standards. Market reforms have been associated with declining access and use of agricultural inputs. This is largely due to the disappearance of credit and input providing state institutions, and the low participation of the private sector in the supply of agricultural inputs and purchase of crops particularly from remote rural areas. Remoteness can be as much a question of "poor infrastructure" and "poor transportation" as of pure distance. It is worth noting the impact that remoteness has (largely through increased transportation costs) in inflating input costs and depressing output prices making the use of purchased inputs, such as improved seeds, inorganic fertilizer and crop protection chemicals, uneconomic. The ratio of average crop producer prices to farm gate fertilizer prices dropped from 1.4 in 1985-89 to 0.4 in 1998 for maize; from 2.2 to 0.6 for paddy; and from 1.6 to 0.8 for wheat (Havnevik, et al 2008).

With very modest increases in labor productivity and yields almost stagnant, Tanzania's agricultural growth has been derived largely from land expansion by farms using traditional technology, with little evidence of improved technical inputs and management practices. (World Bank, 2007) The contribution of agricultural research and extension was limited by several factors. First, services generally focused on increasing production through short-term technical packages, without paying attention to farmers' circumstances, markets, and sustainability. Despite various attempts to strengthen them, the linkages between research, extension and training have remained weak, and collaboration between public and private partners limited. Disproportionate emphasis was placed on generation and dissemination of technology, and less on empowerment (both intellectually and financially) of farmers to adopt the technology. As a consequence of weak linkages within the system, research does not always address priorities of greatest potential impact to the production systems. Technical breakthroughs do not yield good economic returns, and promising technologies remain on the shelf due to lack of knowledge or financing for adoption.

In Vietnam, agricultural development has combined household farming with concentrated areas of larger-scale specialized production. Key supporting policies include land tenure reform (the development of long-term and stable land use rights), high priority for investment in maintenance and extension of the irrigation system, the strengthening of the research capacity feeding into an extension system that transfers new technologies (particular new seeds and breeds) to smallholders, and infrastructure investment which has opened up new areas for the expansion of export crop production (Van Arkadie and Do Duc Dinh, 2004). There has also been progress in reforming agricultural marketing and strengthening processing. While improvements are still needed, a lot more has been done compared to Tanzania. Total government expenditure increased almost fourfold over the 1990s. Agriculture's share of total government expenditure fluctuated from year to year around an average level of 10 percent (Barker et al, 2004). In contrast, reforms in Tanzania attracted support of development partners at a time when priorities within the development community were shifting toward investments in the social sectors. The overall pattern shows a sharp decline in budgetary support to agriculture.

For example, the real allocation to the sector in 1997-98 was about one third the average annual values in the 1991-92 to 1993-94 periods. The 1999-2000 budget was also almost one third lower in real terms than the average of the allocations in the first three years of the period (World Bank, 2000). Vietnamese agriculture is not more mechanized to any great extent, but there is a sharp contrast between the highly intensive irrigated agriculture of Vietnam, and the more extensive, rain-fed agriculture of Tanzania. Over dependence on rain fed agriculture in Tanzania has been a major constraint to sustainable increase in crop production. While there is an abundance of water in rivers and lakes, there is very limited application of irrigated agriculture. Of the 10.7 million ha under cultivation, only 150,000 ha is irrigated representing less than 15% of the estimated irrigation potential of about 1 million ha.

Viet Nam has a clear edge over Tanzania in the effective public provision of basic infrastructure servicing agriculture (notably water and transport). Likewise, the continued functioning of organizations responsible for research and distribution of farm inputs (by a mix of private and public enterprise) underpinned productivity growth - the support system is probably sub-optimal but nevertheless is capable of handling some key developmental tasks, and in general performs at a much higher level than the Tanzanian system.

6.1.3. Industrial Sector Initiatives

In Tanzania, policies that were deployed following economic reforms had mixed results. Reforming the macroeconomic environment had largely worked in favor of the industrial sector especially in stimulating exports, but hurt the sector in terms of high lending rates. Trade liberalization sharpened competition and is perhaps the most criticized policy by local manufacturers in terms of failure of government to promote "fair" competition. While it was intended to promote efficiency, quality and availability of varieties, the form of trade liberalization pursued has seen the promotion of an influx of non-essential imports (thus taxing the foreign exchange base of the nation), and loopholes and leakages (deliberate misspecification of imports and under-declaration). This put competing domestic manufacturers at a disadvantage. Privatization was well intended to address failures of the state in managing public enterprises. Slow progress has been mainly attributed to lack of effective demand by potential local buyers and less attraction to foreign buyers due to accumulated debts and non-viability of the candidate enterprises.

There were a number of instruments and strategies that were missed. The ushering in of liberal reforms in 1986 was supposed to go hand-in-hand with strategies of new technologies and capabilities. However, this came as an afterthought almost a decade later. Even the Science and Technology Policy of 1996 does not address adequately how sectors, sub-sectors or firms could be helped to gain capabilities in crucial areas such as processing, standardization and quality control, packaging, technology adaptation and innovation. The Sustainable Industrial Development Policy (SIDP) of 1996 acknowledges that the labour force in Tanzania's industrial sector is of poor quality, with inadequate technical, managerial, and entrepreneurial skills to meet the challenges of an advanced industrial culture (pp. 25-26), and further that human resources development has not been given emphasis in national strategies (URT 1996). This was an error for which the East Asian experience provides enough lessons.

Poor basic infrastructure (which includes roads, airways, communication etc.) remains a critical constraint to industrial development in Tanzania. Low capacity utilization is associated with poor delivery of services by the utilities such as water and electricity. The supply of these utilities has been irregular, forcing industries to run at sub-optimal levels or incur additional costs of generators and water pumps. No industry can run smoothly in such an environment, hence a contributing factor to the poor performance of the industrial sector in Tanzania despite reforms. Vietnam's pre-reform industrialization efforts seem to have laid the foundation for sustained industrial growth. Part of the difference reflects the human development factor, whereby Viet Nam had a clear lead in terms of investment in human capital.

In the pre-reform period, Vietnam, like Tanzania used State Enterprise as the chosen vehicle for industrial development. The efficiency of the Vietnamese state-owned enterprise (SOE) sector has been subject to criticism, as it is seen to have used a disproportionate share of scarce capital and foreign exchange resources. It has been argued that much of the "success" of this sector reflects large government subsidies, which had negative consequences to the economy as a whole (World Bank, 2004). Nevertheless important segments of the Vietnamese SOE sector, produced successfully and has survived. Vietnamese development is the apparent success of a significant numbers of State enterprises in adapting to the market, entering into joint ventures with foreign investors, changing their output mix, and exporting successfully.

In a decentralized system, many State enterprises competed with each other, having significant autonomy in practice, being owned by many different agencies of the State - all adding up to a social form which was certainly not private capital, but equally in important respects did not conform to the image of Tanzanian monopolistic State enterprises. During the reform period, SOEs in Vietnam have continued to play an important role as part of the "multisectoral economy", through which the government seeks to mobilize all segments of society to achieve high rates of development. Through this policy, both SOEs and private firms are welcome, though the State sector is assigned the leading role. This "leading role" confirms the continuing importance of the SOEs in the Vietnamese economy. This contrast sharply with Tanzania, where a process of dismantling and privatizing parastatals has resulted in the private sector becoming dominant in the Tanzanian economy.

Generally, the private sector is still weak in Vietnam (as indeed it is in Tanzania); so that it was feared that down-playing the role of the state sector would lead to the reduction in the momentum of growth. The reform of SOEs in Vietnam has been carried out through various means, including reorganisation (reducing the number of enterprises substantially), acquisition, selling and lease of some assets. SOEs have been encouraged to participate in joint ventures with foreign investors. Efforts have also been made to introduce greater financial discipline. The abolition of direct subsidies and the end of price controls fairly rapidly exposed State enterprises to much greater competition. While there are still problems of loss-making and inefficiency in many State enterprises, reforms have worked to improve the efficiency of the operations of many enterprises.

7. Impact of External Factors in Supporting Growth

The impact of policy interventions (however good) may be mediated by the exogenous environment. It is argued that powerful exogenous factors contributed to the expansion of the Vietnamese economy (Van Arkadie and Dinh, 2004). The most important would probably be its regional location and the trajectory of the regional economy, and the timing of natural resource (oil) exploitation.

In terms of geography, Vietnam is adjacent to the region which was in the midst of a sustained boom (until the crisis of 1997). There was a spillover of capital and entrepreneurial energy from dynamic neighbors. Moreover, international investors were on the look-out for new Asian Tigers. By comparison, Tanzania, like many other African countries is constrained by geographical disadvantages. Distance from its primary markets and the high transport intensities of her products (low value-high weight and sparsely produced are major impediments to production and trade. Frankel and Romer (1999) find that distance strongly undermines growth due to its impact on international trade. The median transport costs for intra-African trade, at $ 7,600 for a 40 foot container, are almost the same as for imports from the rest of the world (involving much longer distance), and it is $ 2,000 more than for intraregional trade in other developing regions. Nominal freight rates on African exports are normally much higher than those on similar goods shipped from outside the region (AfDB, 1999). For example, freight charges on African exports to the United States as proportion of CIF value are on average approximately 20 percent higher than for comparable goods from other low income countries.

In terms of timing of natural resource exploitation, the development of Viet Nam's oil resources contributed to rapid export growth during the late 1980s and 1990s. In particular, oil revenues came on stream at a critical moment in the transition when Soviet support was faltering. New oil and gas resources continue to be found, and will be significant contributors to economic growth and budget revenue for at least the medium term. In comparison, the mineral boom in Tanzania came much later in the reform process. With the weak performance in other exports, gold and precious stones is now the leading export growth area, and is fast becoming the dominant component in export trade.

8. The Role of Foreign Aid

Donors have played a very active role in Tanzania's development spending throughout the pre-reform and reform periods. Since independence, Tanzania has been one of the largest recipients of aid in Sub-Saharan Africa in absolute terms. Tanzania's share of total aid from all the Development Assistance Committee (DAC) countries was 8.3 per cent during the 1970s, and the country then was the largest recipient of aid in Sub-Saharan Africa. This share started to decline in 1981 and by 1985 it was down to 5.8 per cent. Nevertheless, Tanzania still ranked as the second largest aid beneficiary of aid after the Sudan during the 1980s. More remarkable is that even in the mid-1980s, when the policy environment was very poor in Tanzania, it received more than twice as much as did Ghana, which at that time was considered to be the reformer.

This suggests that there is a high degree of inertia in aid flows. Once they are committed, it is difficult to cut a country loose. Also in the 1990s Tanzania ranked second in SSA, marginally behind Mozambique (Bigsten et al., 2001). More recent trends reveal that Tanzania still receives considerably more aid as a percentage of GDP than most other countries in the region. In 2004, it received around $1.75bn in net ODA (making it the third largest recipient in Africa, in absolute terms), equivalent to almost $48 per capita. This means that in 2004, ODA accounted for over 16% of GNI, and was equivalent to around 40% of government expenditure: 80% of the development budget and 20% of the recurrent budget. More than 50 official donor agencies operate in Tanzania (URT, 2006). Official Development Assistance played little role in the acceleration of growth in Vietnam, and therefore the comparison with Tanzania does not say a lot for the positive impact of ODA. In fact, the period in which reform was initiated with particular vigor and the acceleration in growth began was characterized by sharp declines in external assistance, as support from the CMEA countries collapsed and was not yet replaced by flows from DAC members (Van Arkadie and Dinh, 2004).

9. Private Capital Flows

The role of foreign private capital flows as a source of development finance in both Tanzania and Vietnam has been increasing. There are three main types of private foreign capital flows into these countries: direct investment, portfolio investment and bank lending. The limited development of financial and equity markets has meant that foreign portfolio investment has been insignificant so far in both countries. While that may have limited access to external funding, it also shielded the economies from speculative flows and limited the impact of the East Asian financial crisis in the case of Vietnam. Foreign Direct Investment (FDI) is the least volatile flow and is considered, by far, the most effective for enhancing growth in these countries.

In Vietnam, private foreign direct investment has played a useful role mainly in two ways. Foreign investment, particularly from other economies in the region, was important in promoting the fast growth in labour intensive industrial exports. Foreign investment was also important in providing know-how and finance for the fast growth in energy exports – but with the State Enterprise still playing an important role, most of FDI have been in new investments through joint ventures with Vietnamese firms (80% of projects), and the largest part of it has been in manufacturing.

Tanzania’s comparative advantage in attracting FDIs lies more in its natural resources endowments. Apart from mining and tourism, there is very little export-oriented FDI in other sectors of the economy. Most of the non-natural resource FDI and a majority of privatized firms are geared to supplying the domestic market. FDI flows into infrastructure are still minimal (UNCTAD, 2007).Thus, FDI inflows into Tanzania are predominantly resource seeking, reinforcing commodity-dependent export profiles. This lends FDI into the country a peculiarly enclave character, whereby predominantly green fields and capital-intensive investment is de-linked from the domestic economy and profits are not reinvested. UNCTAD argues that this holds a further danger of state capture by powerful Multi-National Corporations (MNC) interests geared towards resource-extraction at the possible expense of manufacturing interests, thereby undermining diversification strategies. There is also the possibility that large-scale profit repatriation could undermine the balance of payments.

10. Conclusion

The experience of Vietnam provides a few lessons to inform the growth strategies in Tanzania. While both Tanzania and Vietnam economies have responded positively to reforms with steady improvement in economic performance, the level of growth and acceleration in the former has been less dramatic than in the case of the latter. Sustained growth depends on key functions that need to be fulfilled over time: Accumulation of physical and human capital, efficiency in the allocation of resources, and adoption of technology. Although lower levels of investment are important for explaining Tanzania’s slower growth, it is the slower productivity growth that more sharply distinguishes growth performance from that of Vietnam. This situation clearly calls for looking beyond creating conditions for attracting new investors to more explicitly pursuing measures that help to raise productivity of existing and new investment. The paper thus recommends learning from history and from diverse experiences to guide Tanzania’s growth diagnostic work and strategies for scaling up growth.

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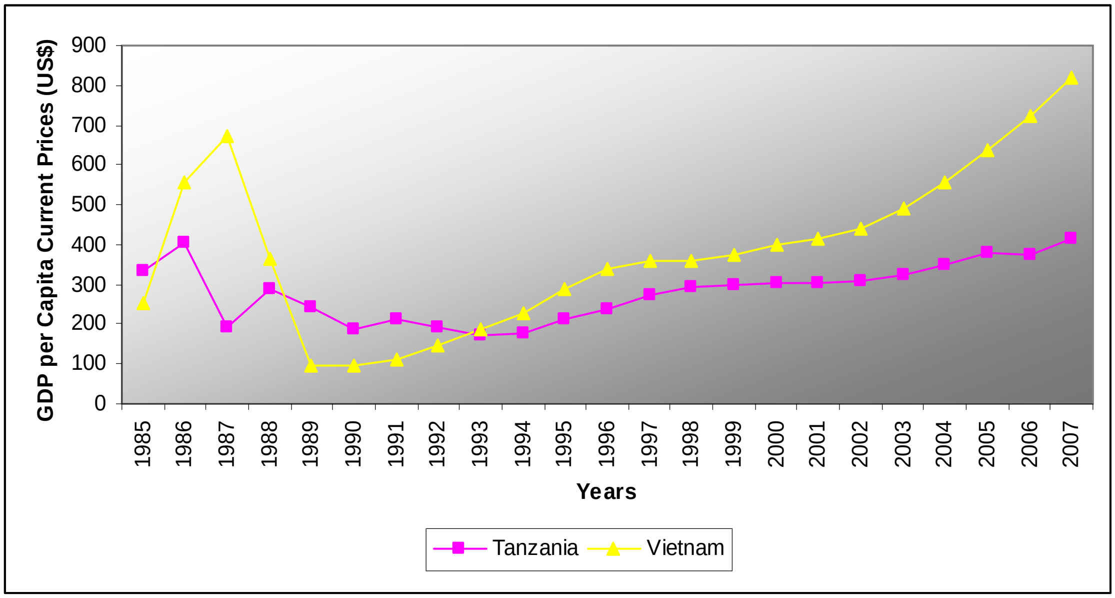
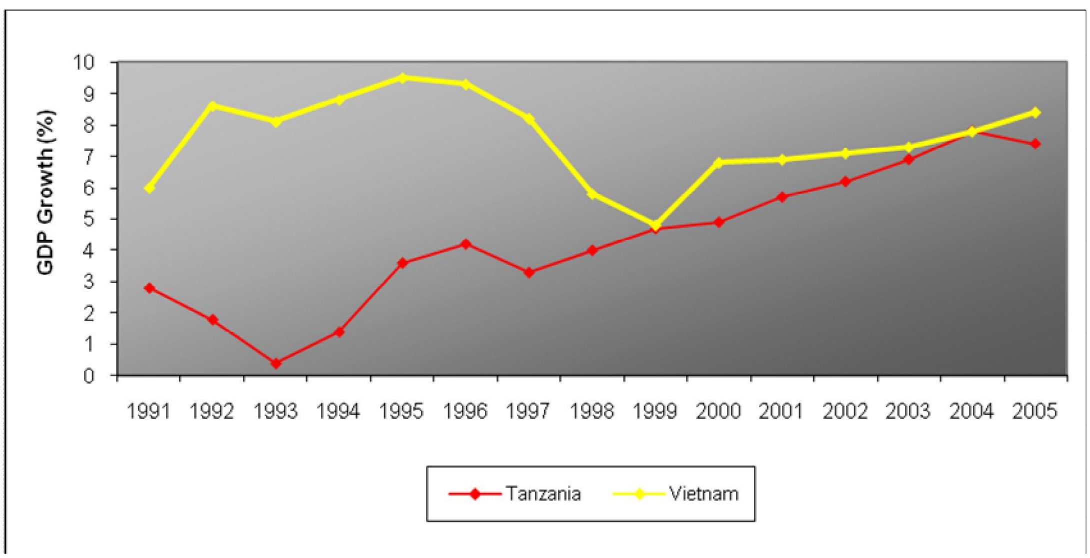
Figure1:Vietnam and Tanzania – GDP Per Capita, Current Prices (US$)



Source: IMF, World Economic Outlook Data Base 2008

Figure 2: GDP Growth in Tanzania and Vietnam (1991-2005)



Source: Vietnam IMF Country Reports (various years); Economic Survey (various years)