

Reflection essay on international finance

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Abstract: The assignment requires one to select one major economic sector in Tanzania and •Evaluate the FDI'S flow and •the importance of FDI's in that sector during the past 4 years. •Identify the likely impairing factors to FDI's in that sector. •Recommend what the government should do to attract more FDI'S Method After selecting the one major economic sector which is

Agricultural sector, data were requested which will provide the end results of this assignment. ? Table of Contents 1. Introduction: Tanzania's Economy4 2.

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References. 12 1. Introduction: Tanzania's Economy Tanzania is one of the world's poorest economies in terms of per capita income, with GDP growth of average 7% per year between 2000 and 2008 on strong gold production and tourism.

However, the economy heavily depends on agriculture, which accounts for more than one-fourth of GDP, provides 85% of exports, and employs about 60% of the work force. Tanzania also depends on the World Bank, the IMF, and bilateral donors to provide funds to rehabilitate Tanzania's aging economic infrastructure, including rail and port infrastructure that are important trade links for inland countries. With the recent banking reforms that have helped increase private-sector growth and investment, and the government has increased spending on agriculture to 7% of its budget.

Continued donor assistance and solid macroeconomic policies supported a positive growth rate, despite the world recession. Also, in 2008, Tanzania received the world's largest Millennium Challenge Compact grant, worth \$698 million. Dar es Salaam used fiscal stimulus and loosened monetary policy to ease the impact of the global recession. GDP growth in 2009-10 was a respectable 6% per year due to high gold prices and increased production. Tanzania's economy was forecast to grow by 7.2 percent in 2012, up from an estimated 6.0 percent this year, provided weather conditions improve as reported by the International Monetary Fund (IMF).

However, Tanzania's economy will grow by a median 6.7 percent this year from 7.0 percent last year, weighed down by chronic energy shortages, as reported by a Reuter's poll. The median forecast by a poll of 11 analysts showed gross domestic product would rebound to 7.1 percent next year in east Africa's second-largest economy. The downside risks to the growth outlook emanate mostly from the power rationing that has been going on in the country. It has compelled firms to resort to less productive sources of power. The Washington-based body earlier this year cut its 2011 growth projection for Tanzania from 7. percent because of widespread power outages triggered by drought in the predominantly hydropower producing country. Africa's fourth biggest gold producer, Tanzania mainly depends on tourism, mining and agriculture and is increasingly attracting higher investor interest in telecommunications, energy, manufacturing, financial services and transport.

2. Evaluation of Tanzania's FDI's flow

The Government of Tanzania (GOT) generally has a favorable attitude toward foreign direct

investment (FDI) and has made significant efforts to encourage foreign investment.

After several years of growing FDI, new FDI declined sharply from USD 6.68 billion in 2008 to USD 2.3 billion in 2009. The number of new foreign projects registered at TIC dropped to 503 last year from 768 in 2008. There is no restriction in foreign exchange. Foreign investors generally receive national treatment; however, the Tourism Act of 2007 bars foreigners from engaging in some tourism-related businesses. The Dar Es Salaam Stock Exchange forbids companies with more than 60 percent foreign ownership from listing.

There are no laws or regulations authorizing private firms to limit or prohibit foreign investment, participation, or control, and firms generally do not restrict foreign participation in practice. The global economic crisis had minimal impact on the Tanzanian financial sector due to its relatively low global integration, however tourist arrivals dropped up to 20 percent, new tourist projects fell by 50 percent, and FDI dropped within the natural resource sector, resulting in layoffs at gold mining firms and stalled mineral and gas exploration and development projects.

The Tanzanian Investment Center (TIC), established by the Tanzanian Investment Act of 1997, is the focal point for all investors' inquiries, screens foreign investments, and facilitates project start-ups. Filing with TIC is not mandatory, but offers incentives for joint ventures with Tanzanians and wholly owned foreign projects above USD 300,000. The review process takes up to 10 days, and involves multiple GOT agencies, which are required

by law to cooperate fully with TIC in facilitating foreign investment, but in practice can create bureaucratic delays.

TIC continues to improve investment facilitation services, provide joint venture opportunities between local and foreign investors, and disseminate investment information. TIC does not have specific criteria for screening or approving projects, but considers factors such as: foreign exchange generation and savings, import substitution, employment creation, linkages to the local economy, technology transfer, and expansion of production of goods and services. Among investment and trade opportunities promoted by the TIC are agriculture, mining, tourism, telecommunications, financial services, and energy and transportation infrastructure.

The Economic Processing Zones Act 2006 authorized the establishment of Special Economic Zones (SEZs) to augment investments in the light industry, agro-processing industry and agriculture sectors. Greenfield foreign direct investments are allowed through this legislation. The Export Processing Zones Authority continues to promote Export Processing Zones (EPZ) to attract investments in agribusiness, textiles and electronics and Spatial Development Initiatives (SDI). Investors in EPZs are eligible for tax exemptions. Investments on the Dar es Salaam Stock Exchange (DSE) are open to foreign investors, but capped at 60 percent.

Foreign investors are barred from participating in government securities. The financial sector has continued to expand, with an increase in foreign-affiliated financial institutions and banks operating in Tanzania. As of December 2009, the Bank of Tanzania listed a total of 27 commercial banks licensed and operating in Tanzania, over half of which are foreign-affiliated

banks. Competition among these foreign commercial banks has resulted in significant improvement in the efficiency and quality of financial services.

Tanzania expected to increase foreign direct investment (FDI) by 16 percent in 2010 from \$645 million last year as the global economy recovers. Foreign direct investment in 2009 dropped from \$679 million the year before as a result of the global financial crisis. The FDI inflows into east Africa's second largest economy were expected to surge to \$800 million in 2011. Tanzania's economy mainly depends on tourism, mining and agriculture. Its telecommunications, energy, manufacturing, financial services and transport sectors are attracting rising investor interest.

It is expected that most of the investments in 2010/11 will focus on tourism, agriculture and telecoms. The government is implementing investment reforms to woo foreign capital. According to the World Bank's Doing Business in the East African Community 2010 report, Tanzania fares poorly in key areas such as closing and starting a business, protecting investors, access to credit, cross border trade and issuance of construction permits. 3. Importance of FDI in Agriculture in the past 4 years Tanzania has more than 44 million hectares of arable land, and a wide variety of ecological zones, climates and water resources.

The country could feed most of the East, Central and Southern African countries with food deficits. 80% of the population in Tanzania lives in rural areas and are in some way or another depending on agriculture. The agricultural sector is vital to Tanzania's economy and therefore also to the reduction and eradication of poverty. Other advantages of FDIs in agricultural sector in Tanzania are as follows:

- Capital: First and foremost FDI brings

much needed capital to Tanzania. This helps the country to achieve rates of domestic investment higher than their domestic savings.

Besides, the financial resources that FDI brings in are in long term and non-debt creating.

- Technology: There are a number of ways in which FDI through TNCs can help develop indigenous technology. Firstly TNCs usually bring in modern technology in agriculture and practices to Tanzania and help it upgrade its existing technology.
- Market Access: TNCs in the agricultural sector has enabled Tanzania to better exploit its comparative advantage in international trade and thus gain access to global markets.

4. Factors Impairing FDI's in Tanzania

- Poor Infrastructure Lack of stable power has led to power outages throughout the country.

It has compelled firms to resort to less productive sources of power. These power outages triggered by drought due to high reliance in the predominantly hydropower. Another significant constraint to improving FDI in Tanzania through agriculture is poor infrastructure within Tanzania. Insufficient investment in the road network has resulted in just 4, 000 kilometers of Tanzania's 85, 000 km road network being paved. Most of these unpaved roads are feeder roads in rural areas, and many routes become impassable after heavy rains. The country's two railway systems are also unreliable, with dilapidated infrastructure and outdated rolling stock. Capacity TIC currently lacks the capacity to address the complicated and non-transparent investment clearance processes, to collect comprehensive and timely data for the research needed to facilitate both policy making and investment decision-making.- Bureaucracy Bureaucratic intransigence continues to pose a severe obstacle to doing business in Tanzania as in the

rest of East Africa. Investors looking to startup businesses in Tanzania often complain about the level of red tape associated with issues such as the issuance of business licenses, company registration, building permits, land certificates and taxation. Corruption is an endemic problem in Tanzania and is often cited as one of the biggest hindrances to doing business. The World Bank 2006 Enterprise Survey indicates that 49.5% of the surveyed companies reports that they expect to make informal payments to achieve specific goals. According to the 2006 IFC-World Bank Enterprise Survey, 20% of the companies surveyed expect to give gifts or make informal payments to get an operating license, and 32% to get a construction permit.

- Seasonality

More than 75% of Tanzanian enterprises are heavily affected by seasonality, whereby farmers sell their produce when prices are lowest and buy inputs for the next cropping season when prices are highest.

- Access to finance Most enterprises in the rural areas are small scale and engage in or rely on agriculture. Bearing the above constraint, these small enterprises have a comparatively high risk, high transaction costs and low volumes, limiting access to capital.
- Regulatory framework The economic growth potential of investments in agricultural land is questionable due to an inadequate regulatory framework governing (FDI) in the sector.

FDI in agricultural sector in Tanzania can even jeopardize local resource users land rights. In such that farmers are giving away their most valuable assets to profit-seeking entities, based on information asymmetries and persuasion.

5. Recommendation to attract more FDI's Including the ongoing reforms to woo investments, TIC continues to improve investment facilitation

services, provide joint venture opportunities between local and foreign investors, and disseminate investment information.

In order to attract more FDIs in the agricultural sector and to increase productivity and high quality output, effort is needed to understand and eliminate the barriers to smallholders that inhibit the growth of productivity. The structural problems facing smallholders such as limited access to information, to input and output and financial markets need rethinking that will attract more FDI to the sector. Such an arrangement would involve smallholders being better organized in producer associations.

Producer associations can improve productivity, reduce costs through supply chain linkages and improve competitiveness. They manage to do so by improving access to necessary and affordable input (technologies and credit). The second challenge is to build integration of production, transport, processing and marketing to take advantage of supply and demand value addition. Third is to ensure the introduction of innovation and knowledge on a continuing basis without subjecting members to high consultancy fees given the socio-economic conditions of smallholders. 6. Conclusion

Apart from general determinants such as macroeconomic stability, efficient institutions, political stability and a good regulatory framework, the smallholder institutional setup has positive impact on FDI flow into the sector. It has been observed that crops whose smallholders are well organized attracted more FDI. An important implication of the result is that FDI to the agricultural sector is not solely driven by policies and incentives to foreign investment and that the institutional setup of smallholder farmers can play an important role in promoting investments to the sector.

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In the short and medium term, efforts to foster integration and creation of strong bonds between smallholders and investors through integrated producer schemes can increase FDI to the sector and thus increase productivity. Other determinants such as investment regulatory frameworks, policies that promote macroeconomic economic stability, and improved physical infrastructure also have a role to play both in the short and long run. In the long run, more FDI can be attained by developing strong institutions in all sectors. ?