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Bank of Tanzania Research Newsletter is an annual publication aimed at disseminating research results of recent studies conducted by staff of the Bank and those done in collaboration with non-BOT staff.

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Inside this Issue

Assessing the Macroeconomic Convergence in The South African Development Community: A Composite Index Approach.

S. Missango, D. Macha, D. Kimolo, M. Sanga and L. Mwankemwa

This study assesses macroeconomic convergence among SADC member states using the Macroeconomic Convergence Index (MCI)—a tool that improves upon traditional methods by offering a comprehensive, longitudinal analysis of convergence trends. While existing approaches provide insights, they lack an integrated perspective on sustained progress.

The MCI, derived from the SADC Macroeconomic the convergence database (2011–2023), incorporates key indicators—inflation, fiscal deficits, public debt, GDP growth, current account deficits, central bank credit to government, and import cover—normalized using a min-max technique for comparability and aggregated into a composite index. Principal Component Analysis (PCA) assigns weights based on economic variance, with sensitivity analyses (including z-score normalization) confirming the index's robustness.

Findings highlight divergent progress: Botswana, the DRC, and Tanzania show significant convergence, while Zimbabwe, Malawi, and Zambia face persistent challenges with inflation, fiscal deficits, and debt management. Overall, regional convergence declined over the study period, largely due to disruptions from COVID-19 and the Russia-Ukraine

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Assessing The Macroeconomic Convergence in The Southern African Development Community: A Composite Index Approach

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conflict, emphasizing the need for adaptive policy measures within SADC.

To address these challenges, lagging economies must tackle structural weaknesses, enhance institutional capacities, and enforce fiscal discipline, potentially through a multi-speed approach that accommodates diverse economic conditions. Strengthening fiscal frameworks and considering a regional fiscal responsibility pact could improve fiscal discipline and debt sustainability. Additionally, better monetary policy coordination is crucial for controlling inflation and managing foreign exchange reserves, which could be supported by enhanced cooperation through the SADC Committee of Central Bank Governors or a formalized regional monetary framework. Accelerating trade and investment integration, improving data quality and harmonization, and addressing structural barriers are also critical. Furthermore, the COVID-19 pandemic underscores the importance of strengthening economic resilience and crisis management to mitigate future shocks. By reinforcing the Macroeconomic Convergence Program, SADC can advance sustainable economic integration, fostering long-term stability and shared growth across the region.

> In achieving macroeconomic convergence, the SADC member countries need to address structural weaknesses, improve institutional capacities, enhance the coordination of Monetary policy and robust fiscal frameworks

Factors Influencing Currency Choices in Trade Settlement in Tanzania

M. Budeba, D. Msafiri, H. Naumanga, E. Makoye, J. Rutahinzibwa, G. Mbiha, G. Mafie, S. Shenyali, and P. Marubili

The U.S. dollar (USD) remains the dominant global currency for trade settlement, despite the emergence of alternatives. Tanzania, like many economies, heavily relies on the USD, making it vulnerable to exchange rate fluctuations and recent USD shortages. This study investigates the factors influencing traders' currency preferences for international transactions and evaluates the feasibility of alternative trading arrangements. Using a mixed-methods approach, including interviews and secondary data analysis, the research highlights the complexities of reducing USD dependency.

> In challenging times, relying on the USD as a primary currency for trade settlement given the exchange rate fluctuations and the USD availability can be minimized through use of alternative currencies for international trade transactions using local currencies of trading countries.

Findings reveal that the USD is the preferred currency for trade settlement due to its global acceptance, stability, and lower transaction costs. However, some Tanzanian traders also use alternative currencies like the Euro, Yuan, Indian Rupee, and Rand when trading with specific partners. Despite this, challenges such as costly currency conversions, high cross-exchange rates, trade imbalances, regulatory barriers, and limited investment opportunities for alternative currencies hinder their broader adoption.

The study underscores the difficulties in shifting away from USD reliance and implementing alternative trading systems. To address these challenges, it recommends policy interventions, including integrating major traded currencies like the Euro and Yuan into Tanzania's Interbank Foreign Exchange Market (IFEM), adopting instant payment systems with key trading partners to streamline cross-border transactions, building trust

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among commercial banks and traders in using local currencies, and further liberalizing the capital and financial account to encourage foreign investment. These measures could pave the way for a more diversified and resilient trade settlement framework.

Unlocking the Tourism Potential of Southern and Eastern Tanzania: Performance, Barriers, and Future Opportunities

Economics Department -Mtwara Branch

This study evaluates the performance of Tanzania's tourism sector in the Southern and Eastern circuits, covering national parks, historical sites, and museums in Lindi, Mtwara, Coast, Ruvuma, and Morogoro regions. Using a mixed-methods approach, the research highlights both growth and untapped potential in these areas. Over the past fourteen years, tourism has shown significant growth, with national park visitors increasing from 63,845 in 2008/09 to 133,935 in 2021/22, and visits to historical sites and museums rising from 114,566 in 2015/16 to 615,663 in 2021/22.

Despite this progress, challenges remain. While 60.6 percent of respondents credited improved road networks for better accessibility, issues persist during the rainy season. Air transport services were deemed adequate, but marine transport, particularly in areas like Bagamoyo and Kilwa, remains underdeveloped. Most respondents were satisfied with essential services such as power, water, health, communication, banking, and accommodation, though 25 percent expressed concerns about the quality of lodging at certain sites. Promotion of tourist attractions also lags, with only 36.3 percent of respondents actively marketing tourism products and 50 percent citing low awareness among visitors and local communities. However, 81.3 percent supported the use of visitor information centers to boost engagement.

To address these challenges, the study recommends upgrading road networks for year-round accessibility, improving marine transport infrastructure, encouraging private sector investment in quality accommodation and services, intensifying promotional efforts, and raising awareness among local communities about tourism opportunities. These measures could unlock the full potential of Tanzania's Southern and Eastern circuits, driving further growth in the sector.

> Enhancing tourism performance in the northern circuit requires enhancing the transport infrastructures both roads and marine, investment in quality accommodation and services, expanding promotional efforts, and raising awareness among local communities.

Horticulture Exports in Tanzania: A Review on Possible Influencing Factors

W. Mbowe, J. Kivamba and A. Mgangaluma

This study investigates the factors shaping Tanzania's horticulture exports, combining desk reviews, surveys, and interviews to analyze trends, challenges, and lessons from peer African countries. Findings reveal mixed performance over the past 15 years, with a notable upward trend since 2014. By 2022, horticulture accounted for 38 percent of total agricultural exports, driven largely by high-value vegetables, which contributed 74 percent of export value between 2014 and 2022. However, diversification into fruits and seeds remains limited, and export market penetration is low, with only 0.5 percent of production reaching global markets due to underreporting and structural barriers.

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Key challenges include production constraints, logistical inefficiencies, limited market access, inadequate irrigation, poor access to quality inputs, and insufficient technical skills. To address these, the study recommends enhancing irrigation infrastructure, strengthening research and extension services, and ensuring timely access to high-yield inputs. Increased agricultural budgets, targeted incentives like subsidies and tax relief, and affordable loans are also critical. Logistical hurdles, such as inadequate cargo planes, high airport fees, and reliance on neighboring countries' logistics, further hinder access to high-end markets. Investments in medium-sized cargo planes, improved storage facilities, and streamlined cargo clearance processes are essential to reduce costs and boost efficiency.

The export chain's dominance by foreign agents limits local traders' market penetration. Facilitating direct access to foreign markets through embassies, umbrella organizations, and FDI, alongside leveraging the African Continental Free Trade Area (AfCFTA), could expand opportunities. Overreliance on a few products like flowers, seeds, and avocados exposes the sector to price volatility. Additionally, limited awareness among farmers and traders about export standards, certifications, and phytosanitary requirements hampers competitiveness. Strengthening training, market information systems, product certification, and digital linkages would attract investment and enhance Tanzania's global horticulture presence. Finally, establishing a coordinating body to align institutional efforts and improve market intelligence is crucial for bridging the gap between producers and markets, ensuring timely responses to emerging challenges.

> To unlock the potential of Tanzania's horticulture exports there is a need to address among others, structural and logistical constraints, also improving market access.

Development of A Viable Blue Economy In Zanzibar

Economics Department - Zanzibar Sub-headquarters

This study evaluates Zanzibar's preparedness to harness its Blue Economy (BE) as a driver of economic growth, poverty reduction, and improved livelihoods. Using primary and secondary data from individuals and institutions across Unguja and Pemba, the research highlights fishing and related activities as the dominant BE sectors, supporting a large portion of the population. However, institutional and capacity challenges—such as limited technical skills, inadequate funding, and weak coordination—hinder the BE's full potential. Environmental degradation further threatens critical ecosystems like mangroves, coral reefs, and seagrass, exacerbated by over-reliance on marine resources, climate change, and population pressures.

To address these challenges, the study recommends strengthening institutional capacity, promoting sustainable resource management, and introducing innovative financing mechanisms like blue bonds, blended finance, and development impact bonds to bridge funding gaps. Additionally, it emphasizes the need for education and training programs to build technical expertise in emerging BE sectors, including aquaculture, marine biotechnology, and renewable ocean energy. These measures could unlock Zanzibar's BE potential, ensuring sustainable and inclusive economic development.

> Sustainable development of the Blue Economy can be enhanced through institutional capacity, promoting sustainable resource management, introducing innovative financing mechanisms, strengthening ecosystem conservation, and promoting public-private partnerships.

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