



## **BANK OF TANZANIA**

### **PRESS STATEMENT**

This week some newspapers wrote stories indicating either that the shilling is in a crisis or that the foreign exchange reserves of the Bank of Tanzania were dwindling. The stories have highlighted a crisis that actually does not exist at all. There is absolutely no need to panic. The Tanzanian economy is very robust: The Government's economic programme adopted in the context of the 2006/2007 budget continues to enhance macroeconomic stability and economic reforms and all the economic indicators are on target, with visible signs of major improvements following the drought of last year.

With regard to exchange rate, Tanzania adopted more than a decade ago a freely floating exchange rate system. The exchange rate of the shilling is determined in the domestic inter-bank foreign exchange market. The Bank of Tanzania intervenes periodically in

case of erratic movements in the exchange rate that are not in line with the economic fundamentals. Also the Bank of Tanzania acts in the market as a buyer and seller of last resort for foreign exchange.

The movement in the exchange rate of the shilling is seasonal, reflecting the demand and supply situation in the market. The movement in the exchange rate follows closely the pattern of inflows of foreign exchange. Normally, the exchange rate depreciates during the period February to July because inflows of foreign exchange are low during those months. The exchange rate stabilizes or appreciates during September to January because of increased inflows of foreign exchange from export crops such as cotton, coffee, tobacco and cashew nuts. It is also during this period that most of donor funds are disbursed. This year the depreciation of the exchange rate has continued beyond July, reflecting a somewhat distorted pattern because of the drought of 2005 and late coming of the main rains earlier this year. The magnitude of depreciation or appreciation during these two periods of the year varies from year to year and depends on strength of export growth and the increase in imports. The magnitude of depreciation of the shilling during past

eight months is consistent with periods in the past when there was a surge in imports. The surge in imports this year stems from the increased cost of oil imports, owing to the unprecedented rise in the price of oil in the world market.

Despite the increased demand of foreign exchange from the surge in imports, the foreign exchange reserves of the Bank of Tanzania have remained high, at about US\$ 2 billion over the last three years. This level of foreign reserves is equivalent to 6 months of imports, which is a higher level than that of most of the neighbouring countries. The coming months will witness increased inflows of foreign exchange and greater stability in the movement of the exchange rate.

It will be noted that the strong macroeconomic policies that the Government has pursued since the beginning of the year, combined with greater availability of food, have succeeded in reducing the annual inflation rate that had reached a peak of 7.7 percent for the year ended May 2006. Thereafter, the annual inflation rate has dropped rapidly to 6.8 percent in June and to 5.4 percent in July. The current economic policies are aimed at reducing the inflation rate

rapidly and thereafter maintaining it at close to 4 percent, a rate that prevailed before the sharp increase in oil and food prices. A low rate of inflation is consistent with a stable exchange rate. Given the strength of the economy, and the Government policies that are in place, the current pressures are transitory and will be well managed.

The Government's economic programme also aims at resolving the current shortfall in the production of electricity through a rigorous and rapid program of increasing the country's capacity to produce electricity from gas. The programme of installing new gas turbines is underway. Given favourable weather conditions in the coming months, the economy should be in a position to resume a more rapid expansion, with a GDP growth rate of at least 7 percent for calendar year 2007.

**Daudi T.S. Ballali**

**Governor**

**Bank of Tanzania**

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