



**Reaping the rewards of foreign
direct investment
Linkages between extractive MNCs
and local firms in Tanzania**

Michael W. Hansen

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LIST OF ABBREVIATIONS

| | |
|---------|------------------------------------------------------------|
| ABG | African Barrick Gold |
| BEST | Business Environment Strengthening for Tanzania |
| BG | British Gas |
| CSR | Corporate Social Responsibility |
| EITI | Extractive Industries Transparency Initiative |
| EPZs | Export Processing Zones |
| FDI | Foreign Direct Investment |
| ICSID | International Centre for Settlement of Investment Disputes |
| IPC | Investment Promotion Centre |
| MDA | Mining Development Agreements |
| MIGA | Multilateral Investment Guarantee Agency |
| MNC | Multinational Corporation |
| MOU | Memorandum of Understanding |
| NBC | National Bank of Commerce |
| NDC | National Development Corporation |
| NGO | Non-Governmental Organization |
| NPV | Net Present Value |
| PPRSP | Parastatal Sector Reform Programme |
| PSSP | Private Sector Support Program |
| SAP | Structural Adjustment Programmes |
| SME | Small and Medium-sized Enterprise |
| SPZs | Special Economic Zones |
| STAMICO | State Mining Company Ltd |
| TDV | Tanzania Development Vision |
| TIC | Tanzanian Investment Centre |
| TRIMs | Trade Related Investment Measures |

ABSTRACT

After a decade of steadily growing foreign direct investment (FDI) in extractives, Tanzania is now facing a virtual ‘take off’ in extractive FDI. One of the concerns related to these investments is whether the foreign investors are linking up sufficiently with local firms through localized supply chains and service inputs. In theory, the opportunities for linkage formation in Tanzania are due to the growing propensity of extractive multinational corporations (MNCs) to outsource sections of their value chain. However, our review demonstrates that linkages in Tanzanian extractives are few and that those that do exist are typically shallow and confined to simple, low value added tasks. The reason for the lack of linkages is mainly that the technology gap between MNCs and local firms is too big to bridge and that a toxic Tanzanian business environment makes contractual partnerships between local firms and MNCs difficult. The lack of linkages amplifies already widespread concerns that extractive FDI leaves too few development benefits for Tanzanian society. As a consequence, pressure is mounting on the government to force MNCs into localizing their value chains through mandatory local content and ownership requirements. The paper assesses the diverging interests and pressures for linkage formation in Tanzanian extractives and discusses whether or not the Tanzanian government will be able to exploit the opportunity offered by the surge in extractive FDI to spur economic development and industrial transformation. The conclusion is that there is a risk that Tanzania will forego this development opportunity due to lack of focused industrial vision and policy.

I. INTRODUCTION

Tanzania is at a watershed in relation to FDI in extractives. For decades, FDI has been confined to gold mining and other smaller operations with limited integration into global value chains. With the discovery of huge gas deposits in south Tanzanian and Zanzibari waters and large uranium, coal, iron and nickel deposits in mainland Tanzania, the country is now facing a FDI *take off* in industrial-use natural resources that may fundamentally transform the Tanzanian economy. All the major players involved, i.e. namely the government, MNCs, local industry and donors, are aware of the significance of the situation and are seeking to position themselves accordingly. The Tanzanian debates on FDI in extractives center around two issues:

1. how to appropriate and distribute rents; and
2. how to promote linkages and spillovers on to the broader economy. In this report we focus on the latter issue.

The paper is based on a perusal of the limited existing literature on Tanzanian linkages and on fifteen interviews with government officials, embassies, business people and researchers conducted in May to August 2013.

In addition, detailed case studies of linkage practices in three large mining MNCs in Tanzania were conducted.

In the following we will briefly describe FDI trends in Tanzania with a focus on extractives and then move on to analyze the scope, content and driving forces behind linkages in Tanzanian extractives.

2. THE TANZANIAN ECONOMY

Over the last decade, Tanzanian GDP growth has been in excess of 6%, one of the highest growth rates in Sub-Saharan Africa (SSA) and a growth rate that over a decade has led to a doubling of national income. This growth is a significant achievement, especially against the background of the stagnant or non-existent growth (when taking into account population growth) during the 1980s and early 1990s. This more recent growth can be attributed to high political stability, widespread institutional reform and not least macro-economic stability. In terms of the latter, and as seen in Figure 1, Tanzania has managed to bring macro-economic imbalances such as inflation, budget deficits and current account deficits under control (OECD, 2013). However, in spite of these economic achievements, Tanzania

Figure 1. Macroeconomic indicators

| | 2011 | 2012(e) | 2013(e) | 2014(p) |
|-------------------------------|-------|---------|---------|---------|
| Real GDP growth | 6.4 | 6.4 | 6.9 | 7.0 |
| Real GDP per capita growth | 3.4 | 3.3 | 3.8 | 3.9 |
| CPI inflation | 12.7 | 16.1 | 8.4 | 6.9 |
| Budget balance % GDP | -6.0 | -9.1 | -3.9 | -3.1 |
| Current account balance % GDP | -11.9 | -11.1 | -11.9 | -10.8 |

Source: OECD 2013. Legend: estimates (e); projections (p)

faces serious developmental and structural problems. While strides forward have been made on the MDGs (UNDP, 2013), Tanzania remains one of the poorest countries in the world. Economic growth has been relatively jobless and accompanied by sluggish improvements in development indicators (Hoffman, 2013). A third of the population live below the poverty line, more or less the same as ten years ago, and living standards for ordinary people measured by GDP per capita have not improved much since the 1970s (Nord et al., 2009). Official figures suggest that a third of young people are unemployed (Therkildsen and Bourgooin, 2012), and the majority of university graduates fail to find formal sector jobs (Curtis and Lissu, 2008).

2.1 Industry structure

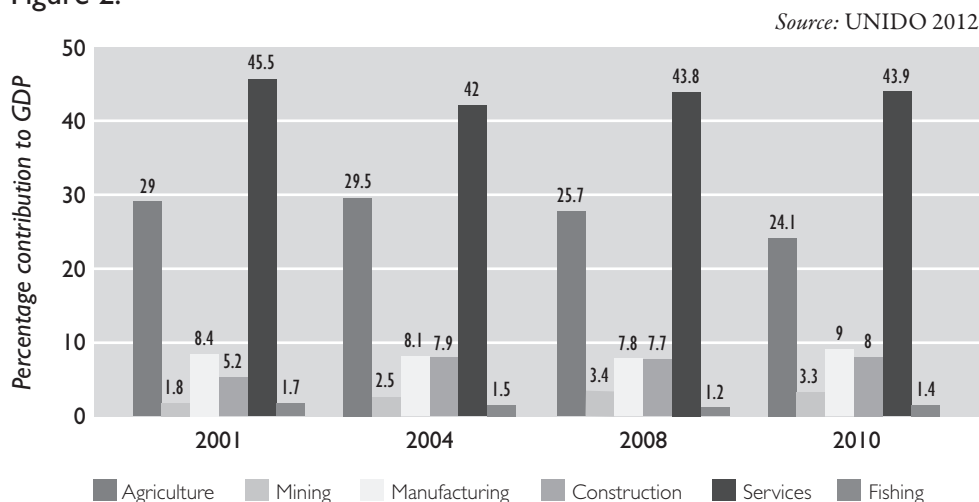
The Tanzanian economy is dominated by agriculture, and although its share of the economy is declining, this sector still accounts for 74% of the labour force. However, it is also characterized by very low productivity which is why this sector contributes less than a quarter of GDP (see Figure 2).

A very large proportion of the Tanzanian economy is informal, and it is estimated that the informal sector accounts for as much as 60 per cent of Tanzania's GDP (World Bank 2005).

The manufacturing sector is small and weak. At 9%, manufacturing is more or less at the same level as in 2001 and below that of other comparable SSA countries (UNIDO, 2012). The manufacturing sector consists of SMEs and a handful of very large conglomerates. The SMEs are involved in food processing (such as milk, meat and fruit processing), textiles and garments, leather and plastics. The large diversified conglomerates are involved in activities such as grain milling, cement, brewing, steel and aluminum and are often spin-offs from trading companies (Sutton, 2012).

Mining accounted for 3.3% of GDP in 2010 and is becoming increasingly important. The discovery of huge natural resource deposits in recent years gives this sector the potential to become a major driver of growth. In particular, large offshore gas deposits are promising; it is estimated that, fully developed, the gas fields could provide 40% of current revenues and 7% of GDP, depend-

Figure 2.



ing on the revenue sharing scheme adopted (Ledesma, 2013). At present, there is no evidence that extractive industries have led to a resource curse in Tanzania: their contribution to GDP is too small, their inflationary effects too modest and their impact on employment too low (Cooksey, 2011a), however the danger obviously exists, as the new generation of extractive development takes off.

2.2 Exports

As seen in Figure 3, Tanzania has become more integrated into world markets, with export and import shares of GDP growing from 37% to 69% during the past two decades (OECD, 2013). The geographical orientation of trade has shifted dramatically over the last ten years, with exports moving away from the EU and the US toward East Asia and Latin America. Also interregional trade has increased, albeit at much slower rates than trade with Asia (see Figure 4). At 10-15% trade in the East African Community is small (UNIDO, 2012).

Exports are largely natural resource-driven, and Tanzania is among the ten most re-

source dependent economies in the world (ADB, 2013). Exports are dominated by traditional ‘soft’ commodities such as cotton, coffee, tea, cashews, sisal and cloves and by hard commodities such as minerals and metals. Export of minerals accounted for 42% of total goods exported in 2009; gold alone accounted for 20% (Morris et al, 2011b) and in 2011 it accounted for 36% of export revenue (Sutton, 2012).

As already mentioned, the manufacturing sector in Tanzania is weakly developed, and consequently Tanzania has historically shown low manufacturing export performance. However, recently it has been pointed out that manufactured exports as a share of total exports have increased significantly (UNIDO, 2012). Indeed, as seen in Figure 4, manufacturing exports as a share of total exports rose from a level of around 25% in 2000 to more than 50% in 2010. However, upon closer inspection it becomes evident that ‘nearly half of the country’s manufactured exports in 2010 were resource-based products (mostly base and precious metal ore). Hence, Tanzania’s manufactured trade performance is not as impressive as it seems at first glance’ (UNIDO, 2012: 27).

Figure 3. Manufactured exports in total exports for Tanzania and comparators, 2000-2010

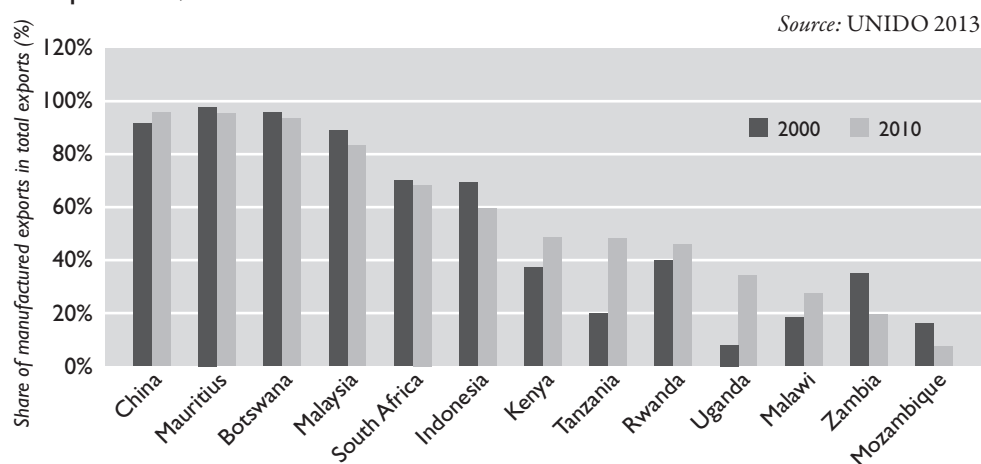
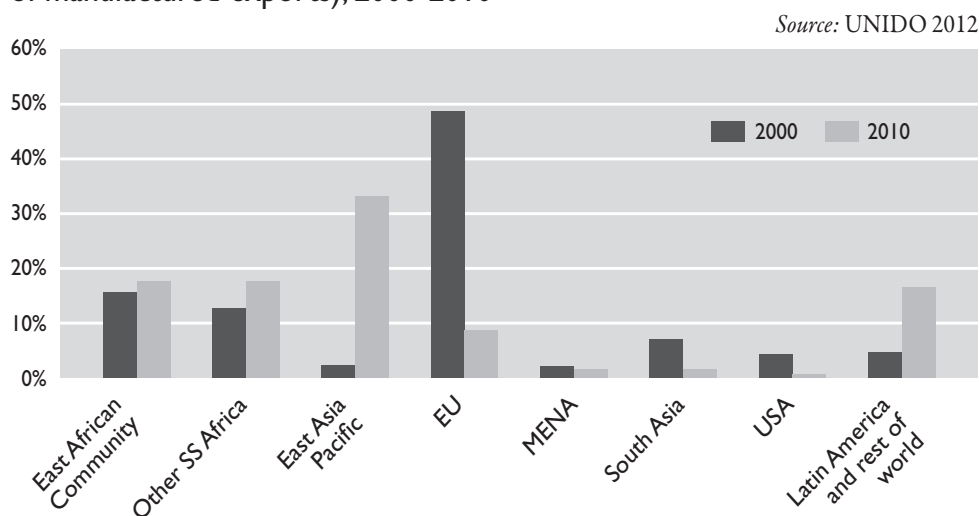


Figure 4. Tanzania market concentration (destinations' share of manufactured exports), 2000-2010



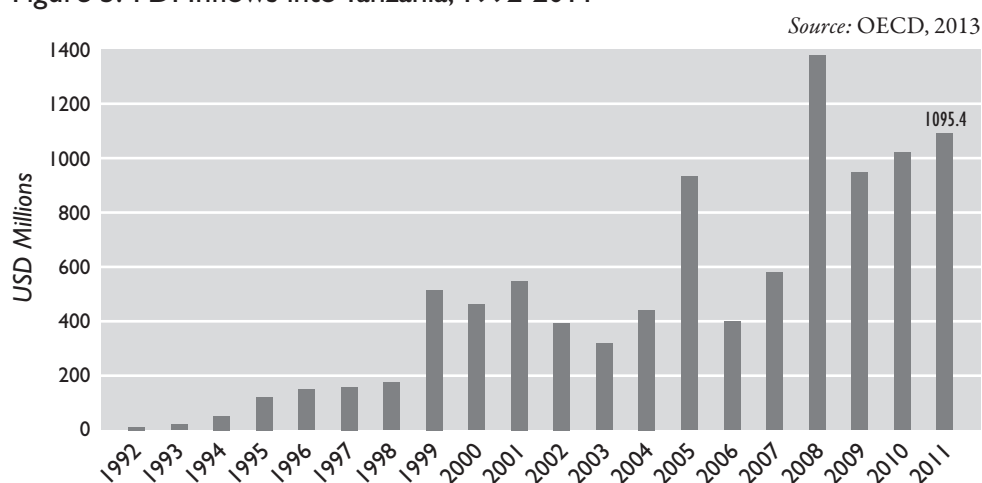
The main manufacturing exports are processed fish, curtains, metal waste and scrap, steel, flour and cut flowers. In other words, manufacturing exports are largely commodity-based, and there is little evidence of exports in traditional developing country manufacturing industries such as textiles and garments, metals and machinery, or electronics. Nor is there evidence that Tanzanian firms are being integrated into global value

chains, apart from providing low value added commodity-based inputs.

2.3 Foreign direct investment

FDI into Tanzania has surged in recent decades, rising from virtually nothing in the early 1990s to a level of around USD 1 billion (Figure 5). But while Tanzania has been relatively successful in attracting FDI, it is

Figure 5. FDI Inflows into Tanzania, 1992-2011



also clear that the country, given especially its endowments in natural resources, has a large unrealized FDI potential (UNCTAD, 2012). Moreover, as a share of GDP, FDI is relatively low (4.6%) compared to other similar African countries, and FDI has stagnated during the financial crises.

The main investors, in order of importance, come from the UK, India, Kenya, Netherlands, China, the US, South Africa, Canada, Germany and Oman (OECD, 2013). In 2008, mining accounted for 27% of FDI, manufacturing for 23% and trade and tourism services for 15% (TIC, 2008). Manufacturing FDI is comparatively small (UNIDO, 2012) and is mainly driven by regional market-seeking investors seeking to jump tariff barriers and reduce transport costs. Virtually no foreign manufacturing investors are using Tanzania as a host for efficiency-seeking investments aimed at servicing global export markets with manufacturing goods.

The largest share of FDI is in extractives. The extractive FDI has largely been dominated by gold investments. Hence, Tanzania is Africa's fourth largest gold producer and, with 2% of known world reserves, the country has a huge untapped potential within gold. USD 2-3 billions have been generated from initial and sequential FDI in gold mining over the years, most of it by large global firms such as the world's largest gold mining firm Barrick Gold (Canada), Anglo Gold Ashanti (South Africa) and Resolute (Australia), all lead firms within the industry. Diamond investments are also large, led by Williamson Diamonds (South Africa) and Tanzanite (AF-GEM, South Africa). Recently, large deposits of industrial minerals (uranium, coal, nickel etc.) have been discovered, and foreign investors have positioned themselves to exploit these resources. In nickel, Kabanga, a joint venture between Barrick and Xstrata Nickel,

had invested more than 200 million in developing a nickel mine near Lake Victoria by 2013. In uranium mining, Australian Mantra is in the process of investing USD 1 billion in developing a mine in the Mkuju River region. Production of coal increased substantially in 2011 when the Ngaka coal fields commenced production. In 2011, China's Sichuan Hongda Co. Ltd. signed a contract to establish a USD 3 billion 80/20% joint venture with the state-owned National Development Corporation (NDC) aimed at developing coal and iron mining in the Mchuchuma region. The largest FDI potential, however, currently lies in natural gas. Natural gas reserves are estimated at 7.5 trillion cubic feet, and at least twelve big companies have been granted licenses to invest in petroleum and gas exploration. Alone in 2013 Statoil and British Gas will each invest USD 500 million in preparation for gas exploitation in Tanzania (OECD, 2013), an amount equal to the total value of FDI in 2011.

2.4 The opportunity offered by extractive FDI

The expected surge in FDI in extractives is potentially a game changer in Tanzanian economic development. High growth may be replaced by even higher growth. A state budget of which 30-35% comes from donors may find other sources of finance, thus decreasing Tanzania's dependence on donors. More generally – and as pointed out by the literature on FDI impacts in Africa (see Morris et al. (2011a, 2011b, 2011c), Amandolagine (2013) or Morrissey (2012) for reviews of this literature) – extractive FDI has the potential to become a key driver of economic and social development through generation of revenues and foreign exchange income and through employment creation, income-generation, and

skills and technology upgrading. But FDI-driven development is a two-edged sword and can also be the source of inflationary pressures ('Dutch disease'), divert resources away from productive sectors with higher job creation and poverty alleviating potential, increase dependency on decision-making at far away corporate headquarters, and cause political and social tensions. A particular problem for natural resources pointed out by the literature is that FDI may become enclaves in the host economy, with no linkages with or spillovers on to the economy at large (Morrissey, 2012). If extractive FDI is to leave a lasting benefit on the Tanzanian economy, it is essential that revenues are extracted and distributed fairly and that linkages are formed with local industry. In particular the latter aspect has received less attention in the recent literature on resource extraction and FDI (Morrissey, 2012). However, as several authors have argued, the formation of linkages with local industries is absolutely key if host countries are to see spillovers and other lasting benefits from FDI (Markusen & Venables, 1999; Blomström et al., 2000; Javorcik, 2004; Günther, 2005; Hansen et al. 2006; 2009; UNIDO, 2012; Amandolagine, 2013). In this paper we will examine the linkage issue from the Tanzanian perspective. We will first look at MNC linkage practices in Tanzania and then move on to discuss the factors shaping these practices.

3. THE BREADTH AND DEPTH OF LINKAGES IN TANZANIA

FDI linkages in extractives are, like all linkages, vertical or horizontal. Vertical linkages are either backward or forward. Backward linkages are collaborations with suppliers of equipment, raw materials or components. They can

also be providers of services such as security services, transport and logistics services, maintenance services, engineering services, etc. Forward linkages are with processing firms, exporters, handlers, distributors etc. Horizontal linkages are linkages with other extractive companies in the same industry, involving, for example, technology agreements with local or international extractive firms, or joint venture collaborations with local (often state-owned) mining companies. Linkages can be measured according to how common they are (breadth) and how intense (depth) (Morris et al. 2011a). 'Breadth' refers to the number and volume of exchanges in linkage collaborations, while 'depth' refers to the degree of exchange of knowledge and reciprocity in the linkage collaboration.

3.1 Horizontal linkages

Foreign investors can work with local firms in the same industry, partly through equity linkages and partly through strategic alliances. To be beneficial to the host country, horizontal linkages require there to be local firms within the same industry that can learn from the foreign investor through direct collaboration or spillover effects such as competition and demonstration effects (Scott-Kennel and Endervick, 2004). There are potentially two types of horizontal linkage present in Tanzania, namely those with small-scale, often artisanal local mining industries and those with state-owned extractive companies.

In gold mining, Tanzania has a sizable artisanal and small-scale gold mining industry (in the following dubbed 'artisanal mining') that was present long before the large foreign gold firms arrived in earnest in the 1990s. This industry used to employ an estimated 500,000 people (Curtis and Lissu, 2008) and accounted for the bulk of gold mining in Tanzania.

Artisanal gold mining is to a large extent outside the official economy and often takes place under horrendous working conditions, with frequent accidents and deaths. While employment in the artisanal gold-mining industry plummeted to approximately 170,000 people in 2007 (Curtis and Lissu, 2008), this industry was still estimated to account for about 10% of total mineral production in Tanzania, with a value of USD 55 million per year. Part of the reason for the decline of the artisanal mining industry was the arrival of foreign investors in the 1990s, which essentially meant that large parts of the artisanal industry were crowded out by larger and more efficient foreign firms. However, the crowding out effect was argued to be due not only to the greater efficiency of foreign MNCs, but also to the preferential treatment given to foreign investors (e.g. in terms of being granted prospecting and mining licenses and tax exemptions) and the outright neglect of local artisanal industries (Bourgouin, 2011; Curtis and Lissu, 2008). A main point of the literature on artisanal mining is that it is very rare to find linkages (e.g. joint ventures, technology collaboration or joint exporting) between foreign mining firms and the local artisanal industry. The few exceptions are that Dalnick Metal Ltd. allegedly increased productivity and facilitated the production of spare parts in Tanzania by leasing mining equipment to local mines (Kweka, 2009) and that a certain level of skills migration has taken place, with, for example, engineers trained in gold mining MNCs moving to local firms (Morris et al. 2011b).

Another form of horizontal linkage in Tanzania is joint ventures with state-owned enterprises. The joint venture collaborations, which were common before liberalization in the 1990s, were typically ‘forced marriages’ in the sense that local partnerships were made a precondition for foreign investment. Thus,

Tanzania formed state-owned extractive corporations that were aimed at building competencies in extractive operations and eventually running them themselves. In oil and gas the Tanzanian Petroleum Corporation was established in 1973, and in mining the State Mining Company Ltd. (STAMICO) in 1972. According to Kweka (2009), little learning took place in these joint ventures, and no Tanzanian extractive corporation reached a skills and technology level where it could undertake mining operations alone (Kweka, 2009). In the case of STAMICO the company failed to maintain adequate levels of reinvestment, and gold production plummeted (Lundstøl et al., 2013).

Mandatory horizontal linkages were abandoned with liberalization in the 1990s, partly encouraged by the World Bank’s recommendations, as stated in a 1992 World Bank position paper on mining (World Bank, 1992). However, recently Tanzania has started reconsidering the role of ‘national champions’ in natural resource extraction. The mining legislation of 2010 opens up makes possible Tanzanian state co-ownership of mining operations (see below), and a number of state-owned extractive companies have been established or re-invigorated. In oil and gas, the Tanzanian Petroleum Corporation has been assigned a key role in the rising gas industry, where it is hoped that joint ventures with foreign MNCs will lead to knowledge transfer and skills upgrading. Similarly, the National Development Corporation (NDC) is designated to play a key role in the development of industrial minerals such as coal and iron.

3.2 Vertical linkages

One way to get an impression of the scope of vertical linkages is to look at indirect job-creation on the part of suppliers and subcontractors. The estimates of indirect job-creation

SHAN TA GOLD (SHANTA MINING CORPORATION)

Shanta Gold is a British and Canadian owned company established in Tanzania in 2001. The company is involved in the exploration, development and mining of gold in five different areas in Tanzania. The company was publicly listed on the London Stock Exchange's Alternative Investment Market and the FTSE sub-sector of Gold Mining in 2005. The initial investment was of USD 76.752 million and there were 100 employees: This has since grown to 950 employees and a total investment of USD 165.680 million. The company has spent considerable time and resources in the exploration phase of its operations, currently operating two mines, and engaged in advanced exploration and development in three other mining areas.

| <i>Estimated procured items</i> | | <i>% out of the total procurement</i> | <i>Local Purchases (%)</i> | <i>Foreign Purchases (%)</i> |
|---------------------------------|------------------------|---------------------------------------|----------------------------|------------------------------|
| Services | Consultancy | 5% | 80% | 20% |
| | Cleaning | 1% | 100% | 0% |
| | Security | 1% | 20% | 80% |
| | Transport | 0.5% | 100% | 0% |
| | Banking | 0.5% | 80% | 20% |
| | Catering | 10% | 2% | 98% |
| Works | Construction | 20% | 10% | 90% |
| | Repair and Maintenance | 5% | 2% | 98% |
| Goods | Capital Goods | 60% | 0% | 100% |
| | Consumable Goods | 5% | 0% | 100% |
| | Not accounted for | 0% | | |

More than 80% of turnover is procurement. The key suppliers for the company have been companies involved in the provision of capital and consumer goods and consultancy services. Most of these suppliers have been dealing with the company for more than 7 years. The key suppliers providing consultancy services have been highly preferred for a long period of time as they provide quality service. By far most of the procurement is foreign. In construction and capital goods, which together account for 80% of procurement, there are almost exclusively foreign inputs. Also catering is more or less foreign. Only in transport, banking and cleaning has it been possible to achieve high local procurement shares. The company acknowledges that in the first phase of exploration the procurement activities were not well organized and no department or unit was set for this function. However when operations commenced in 2011, a department was made responsible for procurement activities. While the government puts pressure via the Mining Act of 2010 in using local suppliers, it is very difficult. There are two reasons why the company has problems sourcing locally: lack of professionalism among suppliers and poor communication (before, during and after contract fulfillment). So far the company doesn't have any initiatives or a policy aimed at developing the local suppliers but the company is planning an intervention to develop the local suppliers.

Apart from the local levies provided to the council authority where it operates, taxes paid and local procurement, no other support is provided to improve the local economy. One of the big challenges related to local communities is local artisans who delay vacating areas acquired by the company for exploration or even invade areas belonging to the company.

Source: Interview, August 2013

in Tanzanian extractives are wildly fluctuating. On the one hand, unconfirmed industry assessments claim that in 2004 gold mining created 8000 direct jobs (including both mine employees and contractors) and 45,000 additional jobs in related and supporting industries, a factor 5-6 indirect employment effect. In preparing its multibillion dollar investment in developing offshore gas extraction of the coast of Lindi and Mtwara, British Gas (BG) has estimated the multiplier effects of their investment using a methodology developed by the ICMM (2011). Here BG estimates that its investment will create 3-5000 direct jobs and more than 8000 indirect jobs. If all direct, indirect and induced effects (income effects) are included, each job at the LNG plant will create five to six additional jobs. BG also predicts that most of the jobs are created in the establishment phase (Hudson, 2013). Other studies of extractives from other countries confirm that extractives often have significant multiplier job effects, although the estimates vary significantly across sectors and countries (McMahon and Remy, 2001; Lundstøl et al., 2013).

Another way to measure the scope of linkages is to assess the share of procurement that is local. We conducted case studies of three major mining operations in Tanzania, namely Shanta Gold, Barrick Gold and Richland. The case studies suggested that procurement (locally bought or imported) is typically very high in Tanzanian mining (between 65% and 85% of turnover). This reflects the fact that mining MNCs have outsourced functions and activities to a very high degree. However, much of the procurement consisted of imported goods. In the case of Richland, local procurement was significant in catering, construction and consultancy, but these accounted for less than a third of total procurement. In Barrick, local procurement

was high in transport, banking, construction and maintenance, but these accounted for less than a quarter of total procurement. In Shanta Gold, local procurement was important in consultancy, cleaning, transport and banking, but these accounted for less than 10% of total procurement. In short, while local firms in Tanzania have made inroads in regard to construction, transport, banking and consultancy, local procurement has been difficult to build in all three cases. Moreover, it is suggested that even these low numbers may be inflated, as local purchases through a local representative office or the dealerships of a global supplier for some MNCs qualifies as local procurement (Hanlin, 2011). At the end of the day, as little as 5% of value added in Tanzanian gold mining may be truly local (Curtis and Lissu, 2008, confirmed by corporate informants).

While there are examples of local linkage formation within mining and extractives and while inroads into certain areas have been made, the general impression from the limited literature is that linkages between foreign investors in extractives and local firms in Tanzania are few and shallow:

- Mjimba (2011), in his study of Tanzanian gold mining, finds that weak, unfocussed and uncoordinated Tanzanian legislation has resulted in very few and mostly shallow linkages from the gold mining operations. Local purchasing only exists in confined areas and in areas where there is low 'complexity' and 'criticality'. Where inputs are 'critical', MNCs prefer to use their international preferred suppliers or alternatively internalize the activity. Even the nominally 'local' firms often had foreign ownership; for instance, although security services were frequently provided by firms domi-

RICHLAND RECOURCES LTD (TanzaniteOne)

Richland Resources Ltd, formerly TanzaniteOne, is a Bermudian registered holding company and is the world's largest miner and supplier of the rare gemstone tanzanite which is only found in Tanzania, in the foothills of Mount Kilimanjaro. Richland Resources Ltd invested USD 56 mill in Tanzania by 2012 and has 670 employees. In 2011, the company made a profit of USD 0.7 million, however, heavy losses were suffered in 2012 partly due to illegal mining activities in the area. The company considers its mining operations to be modern, low-cost operation and boasts an exemplary safety record and it claims to apply international best practice in the design and implementation of its employment, social and environmental policies.

The company procures between 60 -75% of turnover, depending on the stage of the project lifecycle and the level of activity. In 2008, it was decided not to outsource catering, cleaning, transport and security services but to keep it in house. This explains why this company, compared to other extractive firms in Tanzania appear to have relatively low procurement. The company's purchases from external sources are cutting, gemmological equipment and other mining equipment, earthmoving equipment, future, fittings and some improvements to leased premises, infrastructure and surface buildings, motor vehicles, office equipment, raw materials and other consumables used. Most of the suppliers are foreign firms that have the status of key suppliers. These suppliers have typically been dealing with the company for more than 6 years.

| <i>Estimates of procured Items</i> | | <i>% out of the total procurement</i> | <i>Local Purchases (%)</i> | <i>Foreign Purchases (%)</i> |
|------------------------------------|----------------------------------|---------------------------------------|----------------------------|------------------------------|
| Services | Consultancy | 5% | 40% | 60% |
| | Catering, security and transport | 10% | 90% | 10% |
| | Banking | 2% | 20% | 80% |
| Works | Construction | 15% | 100% | 0% |
| | Repair and Maintenance | 5% | 0% | 100% |
| Goods | Capital Goods | 30% | 0% | 100% |
| | Consumable goods- | 25% | 0% | 100% |
| Not accounted for | | 8% | | |

In terms of local procurement, the Mining Act of 2010 and Mining Policy in 2009 of the United Republic of Tanzania require the company to submit procurement plans annually to the Ministry of Energy and Minerals. The annual procurement plans should state in clear terms, the names and nationality of each present supplier of goods and services for each mining project. Although the government does not restrict the mining companies to use local suppliers, Richmond Resources Ltd has provided priority to local supplies in case they meet the required standards and quality desired. However, several challenges have been encountered when dealing with the local suppliers notably; late deliveries or no deliveries at all; poor quality of deliveries; and lack of sufficient capital to honour contracts. However, the company notes that foreign suppliers are not without problems either. For instance, foreign suppliers also have issues with deliveries and in some instances they have lacked flexibility as they had started consider themselves to be the only suppliers.

Richmond Resources Ltd seek to support the local communities in which it operates and in the case of Tanzanite-One Mining Ltd, this includes not only its designated mining area but also the entire district and region. Several initiatives have been undertaken to support the local community, such as bursaries for secondary school students, the construction of a village water plant and a reverse osmosis plant, water supply for primary schools, and construction of roads, police stations and schools as well as a fence for a water pipeline.

Source: Interview, August 2013

ciled in Tanzania, many of these were run by Tanzania-resident South Africans and Zimbabweans. Mjimba finds that only in the exploration phase does it appear that Tanzanian firms – mainly geochemical service firms – have made some inroads so that four out of fourteen exploration firms were Tanzanian. Mjimba speculates that the lower capital requirements in this phase of the investment cycle create the greater inclusion of local service providers.

- UNECA reports that the big gold mining companies AngloGold Ashanti, Resolute and Africa Barrick have their own corporate exploration departments and that local content is limited to drilling services and logistics in exploration and fuel, equipment maintenance, and basic services in mining. Moreover, it is noted that most of the services and goods are imported (UNECA, 2013).
- Kweka, in a study of the gold industry, reports that the mining operations of MNCs have only been integrated into the local economy to a limited degree (Kweka, 2009).
- The Tanzanian Investment Authority (TIC, 2008) reports that the dominant mining investments have “very insignificant sectoral linkage and multiplier effects”, especially when compared to other areas of FDI such as cotton or tourism.
- Diyamett et al. (2011), in a study of fifty mining operations, concluded that in mining, linkages were few and that the MNC operators gained most inputs through imports. The only situation in which technological spillovers took place was through joint explorations between foreign and local mining firms, and training activities.
- Morris et al. (2011b) concluded their study of extractive FDI in eight African countries by stating that Tanzania was the weak-

est performing country with regard to linkages and that linkage development was ‘regressive’ in Tanzania, contrary to most other African countries studied.

While mining MNCs in Tanzania appear to use local suppliers to only a limited degree, they are, as the three case studies suggest, still procuring large quantities of inputs from foreign-owned suppliers, some of whom are located in Tanzania. Mjimba (2011) explains that numerous foreign suppliers have established a presence in Tanzania to be able to service the mining operations. One example is camp management services, where the Sandvik Mining and Construction Corporation supplies drilling machinery through its representative office in Tanzania. This company sold equipment with virtually no local value added. Even food and beverages were sourced internationally. Hence catering services for expatriates and senior mines personnel in the major mines are organized by foreign firms such as Sodexo and All Terrain Services.

3.3 Summary

Overall, it seems that the Tanzanian case, in spite of examples to the contrary, and taking into account the scattered nature of data, resembles a classic ‘enclave’. Horizontal linkages are rare, and the impact of MNC investment on local artisanal producers mainly comes in the form of crowding out. Also vertical linkages appear to be few and shallow, with local procurement limited to low value added and non-critical services such as transport, cleaning and security. Nevertheless, there seems to be evidence of a large potential of horizontal and vertical linkages in the upcoming generation of industrial mining and gas.

AFRICAN BARRICK GOLD (ABG)

African Barrick Gold is a Canadian and British owned gold mining company, operating four mines in Tanzania. The company was established in 2000 and was listed on London Stock Exchange and Dar es Salaam Stock Exchange in 2010. The company's investment in Tanzania has increased from the initial investment of USD 4.2 billion to a current total of USD 6.1 billion. It has also grown from 2020 employees to 5880 since its establishment. The company is mainly involved in the extraction of gold however copper concentrates also result as impurities from the extracted gold. For a period of five years the company has been facing fluctuations in both production and turnover due to fluctuations in the world market prices. The company has been subject to heavy NGO and political attention and has come to epitomize many of the problems related to gold mining in less developed countries. Whether the fact that Barrick has spun off its Tanzanian operation in a separate company and has been seeking to sell it off is related to these NGO campaigns or rather to the fact that the Tanzanian operation, according to internal Barrick figures, is the most costly among its numerous activities around the world, is not known.

The company has outsourced most activities in recent years, and now procure 80-85% of turnover. Transport contraction and maintenance are to a significant degree sourced to local providers, banking to a lesser extent. Overall, local sourcing accounts for little more than 20% of total procurement. In 2010, the supply chain was centralized to a large supply chain department with its own directorate. As a consequence, the company's global supply base has been reduced from 2500 to 2000 suppliers, thus reducing costs. The company's key suppliers are those who supply capital goods and consumer goods. These have been in a position to deal with the company for more than 10 years, so they understand the company specifications.

| <i>Procured Items</i> | | <i>% out of the total procurement</i> | <i>Local Purchases (%)</i> | <i>Foreign Purchases (%)</i> |
|-----------------------|------------------------|---------------------------------------|----------------------------|------------------------------|
| Services | Consultancy | 10% | 2% | 98% |
| | Cleaning | 5% | 0% | 100% |
| | Security | 1% | 0% | 100% |
| | Transport | 0.5% | 100% | 0% |
| | Banking | 2% | 20% | 80% |
| | Catering | 10% | 2% | 98% |
| Works | Construction | 10% | 100% | 0% |
| | Repair and Maintenance | 10% | 50% | 50% |
| Goods | Capital Goods | 15% | 0% | 100% |
| | Consumable goods- | 30% | 0% | 100% |
| Not accounted for | | 23% | - | - |

The company has initiated local procurement programmes, partly in response to the strong pressure the company has been under from NGOs and government. However, the company raises some concerns when dealing with local suppliers notably; poor communication. For instance, in a procurement of branded shirt uniforms (a contract of around USD 200,000), the supplier was contacted by email but lost the contract as it did not respond to the email. The local suppliers lack professionalism in the way they conduct their business practices not respecting the contract terms. Moreover, the quality of the goods or services offered by most local suppliers is low standard and often prices quoted are inflated unnecessarily. Lastly local suppliers lack capital to finance delivery on contracts. Seeing the challenges raised above Barrick has sought to assist e local suppliers to improve performance and a desk has been set aside to deal with both international and local key suppliers. The company has undertaken the following supplier development initiatives: seminars, one to one meetings, training on business ethics, preparation of supplier guide book, and provision of financial support by paying in advance before delivery (paying them within two weeks instead of four weeks). The company notes that there are also problems with foreign suppliers. It would be helpful if government ensure all suppliers are registered and recognized and create a unit responsible for listing and blacklisting all suppliers in the country.

The local community and NGOs have increasingly been putting pressure on Barrick to ensure larger contributions to the local community. There have been several uprisings such as strikes, sabotages and invasion of the mines. As a result Barrick has become involved in a number of activities aimed at boosting the capacity of the local community such as the construction of hospitals and schools, sponsoring education of employees, support of a number of local programs through the "Maendeleo" Fund (Development Fund).

Source: Interview, August 2013

4. FACTORS SHAPING LINKAGE FORMATION IN TANZANIA

In the following, we will search for explanations for the current state of linkages in Tanzania and identify factors that may promote a broadening and deepening of linkages in Tanzanian extractive sector in the future. We will argue that the scope and depth of linkages depend on four sets of factors and their interplay, namely local factors such as government and local industry factors, as well as foreign factors such as MNC- and donor-related factors.

4.1 Government influences on linkage formation

4.1.1 General industrial policies and strategies

Industrial policy in Tanzania is a textbook example of ambitious state-led industrial development plans that collapsed in the face of economic fundamentals and was replaced with almost their opposite, highly liberal open-door economic policies. In recent years, the Tanzanian government has sought to re-formulate its industrial policy to make it more targeted and to ensure that the private sector contributes more effectively to development objectives such as job creation and skills development. Hence, the government has adopted an array of plans for developing the private sector, including Big Results Now, the First Five Year Development Plan (2011/12-2015/16), Tanzania Development Vision (TDV) 2025, the 2005 Mini Tiger Plan and the latest, the Integrated Industrial Development Strategy 2025. A plethora of generic plans and a similar multitude of sector-specific plans related to Trade, SMEs, EPZs, Agriculture, Tourism and Mining should be added to this. The combined aim of all these poli-

cies is to turn Tanzania into a middle-income country by 2025. FDI plays an important role in these industrial development visions, strategies and policies. And just as the general industrial policy framework has moved from state dirigisme in the 1960s-1980s via liberalization in the 1990s and 2000s towards more assertive approaches in recent years, industrial policy as it relates specifically to foreign investors has moved from restrictive approaches via 'passive open door' approaches towards 'selective targeting' approaches very recently.

Tanzania is notorious for its early state-led industrialization strategy. In 1967, Tanzania adopted the Ujamaa policy as part of the Arusha Declaration, essentially a socialist policy of state dirigisme and self-reliance. It prescribed the nationalization of major economic sectors, the indigenization of 'foreign interests' (including those of non-ethnic African origin), self-reliance and the introduction of economic planning according to socialist principles (Therkildsen and Bourgooin, 2012). In connection with Ujamaa, the Tanzanian state sought to control the extractives sector, allowing in only a few foreign investors, and even then only as partners of the state-owned mining corporations. The Ujamaa policy collapsed in the early 1980s due to serious current account deficits, partly caused by an increasingly unproductive state-controlled sector. As a consequence of the economic crisis, Tanzania was made subject to Structural Adjustment Programmes (SAPs) formulated by the IMF and the World Bank. The SAPs prescribed, among other things, the removal of subsidies, the privatization of state-owned enterprises, export promotion, deregulation, the removal of trade controls and the liberalization of foreign exchange.

By the mid-1980s, Tanzania embarked on a reform programme that fundamentally broke

with the socialist past, implying the rolling back of state planning and opening most sectors up to private investment, foreign as well as domestic (Nord et al., 2009). In 1992, with donor support, Tanzania adopted an ambitious privatization programme – the Parastatal Sector Reform Programme (PPRSP) – which led to the mass privatization and divestment of the then approximately 400 parastatals (Mjimba, 2011), including the national brewery and cigarette, soft drinks and cement companies.

4.1.2 Foreign direct investment regulation

As part of the deregulation and privatization efforts of the 1980s and 1990s, Tanzania undertook a radical change in its approach to FDI. Restrictions on foreign investors were gradually removed and various measures to promote FDI initiated. In 1990 Tanzania approved a National Investment Promotion Policy and Investment Code and established the Investment Promotion Center (IPC). In 1997 this early investment regulation was replaced by the Tanzania Investment Act, according to which Tanzania was opened up to investors in most sectors. The legislation actively promoted FDI through import duties and VAT exemption on capital goods, as well as import duty drawback schemes. The legislation further allowed for foreign investors to use expatriate staff depending on the sector, and it guaranteed repatriation of profits and earnings. Investment became guaranteed against expropriation, and Tanzania became a member of the WTO in 1995, the International Centre for Settlement of Investment Disputes (ICSID) and the Multilateral Investment Guarantee Agency (MIGA). As a consequence, National Treatment (treating foreign goods no differently from domestically produced goods) was extended to most

industries and sectors. The reforms also established the Tanzanian Investment Center (TIC) to replace the malfunctioning IPC. The ambition was that the TIC should become a one-stop center aimed at promoting and coordinating investments. To further attract export-oriented foreign investors, Tanzania established a number Export Processing Zones (EPZs) and Special Economic Zones (SEZs). The EPZs were regulated through the Export Processing Zone Act of 2002 and sought to transform local supplies into exports through various local procurement and export incentives. SEZs were regulated through the Special Economic Zones Act of 2006 and designated special economic zones as objects for FDI. As a consequence of all these reforms, Tanzania ended up with a highly open FDI regime with unconditional repatriation of profits, license fees, remittances from expatriates, etc.

Specifically for mining, the 1990 Investment Promotion Policy removed the requirements for government participation in mining. In 1994 a Mining Sector Policy Framework was set up, stipulating the divestment of state-owned mines, reforming the regulatory framework, establishing a fiscal regime to govern mining and strengthening institutional capacity in the Mineral Resource Department. According to Butler (2004), the liberal stance on foreign investments in mining was inspired by recommendations made by the World Bank in the 1992 ‘Strategy for African Mining Technical Paper’ (World Bank, 1992). This paper criticized the previous local content, local employment and local ownership requirements and specifically recommended the state not distinguish domestic from foreign investors and not use mining as an engine of employment generation. The World Bank provided institutional and financial support for reforms along the

lines suggested in the paper. While, as argued by UNIDO (2012; 19), “the liberalization agenda the government has diligently followed since the 1990s has paved the way for major investments in several resource-based sectors”, concerns regarding these liberal policies mounted during the 2000s. As a consequence of these concerns, by the mid-2000s the Tanzanian government started contemplating a more assertive approach to extractive FDI. The new approach focused on two issues: 1. How to increase revenues through taxation; 2. How to promote linkages with the local economy.

4.1.3 Gaining revenues from FDI

In the wake of liberalization in the early 1990s, Tanzania introduced provisions for the taxation of mining investors as well as clauses stipulating exemptions. Tanzania therefore sets requirements for corporate income tax, royalties, a withholding tax, exemptions from indirect taxes and deductions for capital investments. While these impose both costs and gains for foreign investors, the measures were formulated in a situation in the 1990s when Tanzania was eager to make the country more attractive to foreign investors. The focus on FDI attraction resulted in what, according to many observers, were too low revenues from extractive FDI. For instance, in the Financial Year 2006/2007, exemptions for gold mines had a value of USD 769 million and of USD 538 million the following year (Cooksey, 2011a). This contrasts with total tax paid between 1997 and 2007 of USD 429 million. Lundstøl et al. (2013) estimate that the Tanzanian mining sector has historically generated less than its potential revenue. At the minimum it would be expected that revenues would have a similar share of total revenues as the sector’s share of GDP, but at

2.3% of revenues compared to 3.1% of GDP on average in 2008-2011, revenues fall short of this expectation. Lundstøl et al. (2013) calculate that potential revenues in Tanzania are 136% higher than actual revenues.

The below-potential revenue can be attributed to widespread tax exemptions and deductions as well as ineffective tax collection. Likewise, there have been concerns regarding arbitrary decisions, delays and a lack of appeals in cases involving Tanzania’s taxation of mining (Cooksey, 2011a). Moreover, several authors point to rent-seeking by authorities as a cause of low revenues. Cooksey and Kellsall (2011) report on the so-called Alex Stewart gold audit corruption case which involved key public officials, as well as the Meremeta Ltd. case, where gold and mining purchases were used to finance military procurement. Similarly Curtis and Lissu (2008) imply that Mining Development Agreements (MDAs) have been subject to rent-seeking practices, thus diverting government revenues into private pockets and/or leading to lost revenues for the government.

The lack of revenues from minerals FDI motivated a number of government studies and commissions during the 2000s, culminating in the new Mining Act in 2010. This legislation removed some exemptions, increased royalty and taxation levels, and enabled government shares in extractive operations free of charge (Lundstøl et al., 2013). However, these reforms will only impact on revenue in the longer term, as ‘financial stabilization clauses’ (clauses that stipulate legislative and contractual financial responsibilities of the contracting parties as part of MDAs and that are subject to investment arbitration (OECD, 2013)) obviously constrain the ability to generate additional revenue in already contracted concessions. Tanzania also created a semiautonomous mineral audit agency

(Lundstøl et al, 2013) to address the problems related to corruption and rent-seeking. Finally, Tanzania signed up to the Extractive Industries Transparency Initiative (EITI), which promotes accountability and transparency in extractive industries. While it is too early to draw conclusions regarding the effectiveness of these revenue-generating measures, recent government figures suggest a 59% increase in revenue generation from mining between 2011 and 2012 (Guardian, 14/7 2013). Moreover, depending on the revenue-sharing schemes adopted in the upcoming gas and mining projects, government revenues from extractives are projected to become the most important source of government revenue in the future (Ledesma, 2013).

4.1.4 Promoting linkages with the local economy

As mentioned above, Tanzania's FDI and mining legislation takes a rather liberal approach to foreign investors. Nevertheless, the government has made attempts to promote linkages. For instance, the 1998 Mining Act says that the act should assist in developing the country's ability to provide inputs to the sector. The act also makes possible the promotion of forward linkages, as well as incentives for the development of local value-adding activities. There are provisions for succession programmes, that is, specific programmes for gradually replacing foreign expatriates with local employees and reserving certain parts of the exploration cycle (e.g. prospecting licenses, reconnaissance, mining licenses and special mining licenses) for local Tanzanian companies, defined as companies that are solely owned by Tanzanian citizens. However, all subsequent licenses can be solely foreign, and the local licenses obtained in the exploration phase can be sold to foreign

firms, provided they engage in joint ventures with the local firm. The 2010 Mining Act further stipulates that MNCs seeking prospecting and mining licenses are expected to draw up lists of goods and services that can be provided by local firms, something that may enhance opportunities for local firms to serve as suppliers to the foreign investors. The act also promotes horizontal linkages. Hence, according to the act, the Minister of Energy and Minerals can now require foreign companies to give the government a free owner share in return for a Mining Development Agreement (MDA). Finally, there are provisions to facilitate the establishment of training institutions to develop industry-supporting skills, as well as to encourage foreign investors to contribute to the development of skills and capabilities.

However, it is noticeable that there are no mandatory provisions for linkages in the Tanzanian mining legislation. By avoiding mandatory requirements such as local content requirements, Tanzania no doubt avoids conflict with the provisions of the WTO TRIMs agreement (Trade Related Investment Measures), which considers trade-related performance requirements as breaching the National Treatment Principle. Moreover, the provisions that do exist are all vague, and the process of forming linkages is largely left to market forces. As Mjimba argues (2011), the problem is that the Mining Act lacks specific targets, monitoring mechanisms or incentives and sanctions related to reaching the overall development objectives. Even though the Mining Act mentions the importance of training and technology institutions, it fails to establish effective provisions for developing local capacity in the mining field. Moreover, other parts of the Tanzanian investment framework directly counter local linkage development. Hence, the Mining Act stipulates

employment, VAT and duty exemptions for foreign investors, as well as duty drawback schemes for imports of capital goods and other goods and services. This obviously provides a disincentive to foster local linkages and puts local suppliers at a disadvantage, as they do not have access to such exemptions. In fact, local suppliers face a ‘double disadvantage’, as they not only face higher tariffs but also have to operate in a deficient Tanzanian business environment. These policy inconsistencies have made several observers conclude that the lack of linkages and the shallow nature of linkages can mainly be attributed to the policy regime (Mjimba, 2011; Kweka, 2009).

The lack of specific and mandatory provisions for linkages in Tanzanian legislation has drawn a lot of criticism over the years, and recently change seems underway. Hence local content and ownership requirements are contemplated as part of several pieces of legislation under preparation, including the Gas Act, the Minerals Act, the Land Legislation Act and the Investment Road Map exercise.

4.1.5 Business environment

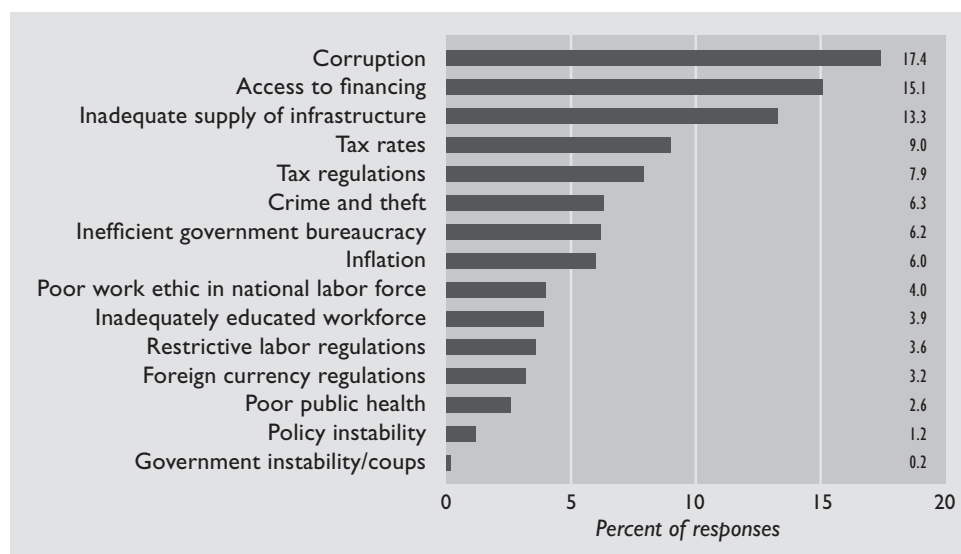
Linkage formation is not only affected by specific linkage measures, but also by the quality of the general business environment. While the business environment has been high on the agenda since the late 1980s and numerous initiatives have been implemented to improve it, the Tanzanian business environment remains among the worst in Africa. Where some countries have made huge strides forward – for example, Ghana moved from 101 to 65 in the World Bank’s Doing Business Index – Tanzania stagnated. Hence, the World Bank ranked Tanzania 125-140 out of 183 countries from 2005-2012, and it even slid backwards over this period (see Figure 6). Likewise, the Global Competitiveness Report (2011/12) ranked Tanzania 113 out of 139 countries. The IMF has suggested that the problems related to the Tanzanian business environment consist of “burdensome licensing procedures, reflected in high start-up costs, insufficient access to credit, restrictive labor regulations, difficulties in registering property and poor property rights, and very poor infrastructure” (IMF, 2006; 9). An

Figure 6. Tanzania’s Overall Ranking in Ease of Doing Business

| Doing Business (DB) Report | DB 2009 | DB 2009 | DB 2009 | DB 2009 |
|-----------------------------------|---------|---------|---------|---------|
| Overall Rankings | 126 | 131 | 125 | 127 |
| Starting a Business | 111 | 120 | 122 | 123 |
| Dealing with Construction Permits | 175 | 178 | 177 | 176 |
| Employing Workers | 133 | 131 | 80 | 78 |
| Registering Property | 145 | 145 | 155 | 158 |
| Getting Credit | 84 | 87 | 96 | 98 |
| Protecting Investors | 88 | 93 | 93 | 97 |
| Paying Taxes | 113 | 119 | 123 | 129 |
| Trading Across Borders | 105 | 108 | 115 | 92 |
| Enforcing Contracts | 31 | 31 | 33 | 36 |
| Resolving Insolvency | 113 | 113 | 120 | |

Source: World Bank Doing Business

Figure 7. The most Problematic Factors for Doing Business



Source: ADB 2013

AfDB (2013) survey among business experts and leaders found that the main problems with the Tanzanian business environment are related to corruption, followed by financing and taxation. Infrastructure, inefficient government bureaucracy and a lack of education and skills in the work force also rank high on the agenda (see Figure 7).

Looking at the business environment for extractives specifically, the Fraser Institute of Canada assesses the quality of mining jurisdictions around the world. According to this, Tanzania has a very large mining development potential but needs to establish good institutions to manage these resources. However, the actual quality of Tanzania's minerals resource management has made the country slide from a position as number 48 in 2004-2005 to a position as number 68 out of 71 jurisdictions in 2008-2009 (Cooksey, 2011a).

The problems of the institutional environment surrounding extractive FDI may have serious repercussions for FDI level, profile and impact. First, a difficult business environment may affect the relative attractiveness

of Tanzania compared to other natural resource-rich locations and lead to foregone investments, thus reducing linkage opportunities. Second, a difficult business environment may severely undermine efforts to form linkages with local industry. This aspect is often overlooked in the debate over the influence of business environments on FDI. A difficult business environment may constrain the development of viable local supplier firms; indeed Perkins and Robbins (2011) argue that the limited extent of linkages in Tanzanian mining can be attributed to a bad business environment and infrastructure shortcomings which curb development of the domestic enterprise sector. Moreover, a difficult business environment may render contract-based collaborations between MNCs and local firms difficult to establish and maintain due to inefficient contract enforcement institutions and uncertainty regarding contracts.

Donors have put strong pressure on the Tanzanian government to improve the business environment, and organizations such as SIDA, DFID, DANIDA and the World Bank

have invested heavily in doing precisely that, for instance, through the multidonor BEST programme (Business Environment Strengthening for Tanzania) and the World Bank Private Sector Competitiveness Project (2006). As part of the efforts to improve the business environment, the government has initiated the so-called Road Map exercise headed by the Prime Minister's office, which has a coordinating role. In spite of all these efforts, however, huge problems remain, as described above.

The fact that the business environment remains feeble in spite of all efforts to improve it offers an enigma to outside observers, as it would seem that Tanzania, with relatively small investments, could gain huge economic benefits. One reason for the lack of progress seems to be a lack of any sincere political commitment to improve the business environment. As Cooksey argues (2011a; 76), "It is routine for senior officials, from the President downwards, to express concern with the (invariably critical) points raised by donors, with promises of action. This invariably involves delegation to subordinates, and usually nothing much happens thereafter". Informants at western embassies trace the problems back to a left-over mentality from the Nyerere era, where, in spite of the market-friendly rhetoric, the private sector is viewed with great suspicion. Another explanation offered is that politicians and administrators have become complacent with regard to business environment reform since investment levels, as suggested earlier, have surged over the last decade.

4.1.6 Politicization of linkages

The extractive industry, especially gold, has been politicized for a long time, and the past history of gold is to a large extent shaping the current debates on gas and industrial use extractives. The liberal approach to for-

eign investors adopted in response to the collapse of Ujamaa has drawn heavy criticism in recent years, and political pressure for a more assertive approach to FDI has mounted. Foreign MNCs are broadly perceived as crowding out local artisanal mines, extracting ("unfair") tax exemptions from the government and causing social and environmental disruption in local communities. For many, Tanzanian gold mines, especially those controlled by Barrick, have epitomized the negative consequences of extractive FDI in less developed countries, and the mining companies have been subject to intense campaigns from local and especially international NGOs (see Cooksey (2011a) for an overview). During the 2000s, Tanzania witnessed highly politicized conflicts surrounding gold mining over, for example, evictions of artisanal miners from land acquired by mining MNCs and the perceived low revenues from extractives.

The politicization of extractives in general and of linkages in particular has intensified recently in connection the discovery of huge gas deposits in south Tanzanian waters. In May 2013, riots sparked by the government announcement that gas finds would be diverted from Mtwara to Dar es Salaam left six people dead. The Lindi and Mtwara communities, which are the closest regions to the planned offshore operations, have argued that gas should be used and processed in their regions, rather than being transported through a pipeline to Dar es Salaam. The conflict revealed cleavages not only between regions but also between parties and along religious lines. The leader of the opposition party, the CUF – a party that is mainly supported by Muslim constituencies – has announced that the distribution of benefits from gas exploitation will be a key theme in the 2015 election campaign. Opposition legislators are also try-

ing to delay approval of the planned pipeline to Dar es Salaam. For whatever reason, the adoption of a Natural Gas Policy has been delayed, and there is no expectation of it being approved before late 2013.

The politicization and indeed radicalization of the linkage issue is of deep concern to investors, who hitherto have been able to rely on the high level of political and macro-economic stability in Tanzania and on a firm government commitment to investment promotion and protection. However, this may change in the future as political competition for the spoils of extractive FDI intensifies. BG and Statoil's delaying of the final decision to invest in a USD 15 billion LNG plant until 2016 may partly be related to uncertainties regarding the political environment in Tanzania for oil and gas extraction.

Thus, the Tanzanian government is facing a very difficult balancing act. On the one hand, it is aware that any change in the current regime may scare away investors, wary that their investments may be rendered unprofitable by stringent new requirements; Cooksey (2011a) argues that the anti-MNC rhetoric and the more assertive policies adopted by President Kikwete since the mid-2000s may already be affecting the attractiveness of Tanzania for investors. On the other hand, the government needs to satisfy constituencies wanting a stake in the development and growth opportunities provided by the surge in extractive FDI. With the discovery of large deposits of natural resources and the high prices for them, the Tanzanian government seems increasingly assured that its bargaining position with MNCs is being strengthened and that it can and should step up pressure on the extractive sector. Hence, the government is currently revisiting its relatively liberal investment regulation in order to promote broader development effects.

The political economy of linkages is in many respects a micro-cosmos of the political economy of industrial policy in Tanzania. Several studies have described and analyzed the evolution of Tanzanian industrial policy (see e.g. Therkildsen, 2011; Therkildsen and Bourgooin, 2012; Cooksey, 2011b). A common thread in this literature is that over a very long time span Tanzanian politics has consistently been able to deliver stability and legitimacy, while being less successful in creating the conditions for the development of productive sectors. Tanzania is characterized by a high degree of stability, and the ruling coalition supporting the CCM (previously TANU) has been able to keep the latter in power over almost fifty years, which is an achievement, not least given the fact that since 1995 Tanzania has had competitive elections. This stability can be explained with reference to the ability of the government to form coalitions of the major interests within the ruling party, as well as coalitions with major social interests (Therkildsen, 2011; Therkildsen and Bourgooin, 2012). However, while the government has promoted stability, it has also, as demonstrated above, been unsuccessful in promoting a broad-based and job-creating industrialization process in Tanzania. One reason could be that the interests of private enterprises have been weakly represented in the political process. This is partly related to the ethnic dominance of Tanzanians of Indian and Arab origin in the private sector, which may have made the government unwilling or unable to adopt private sector-friendly policies in the past (Therkildsen and Bourgooin, 2012). A second reason is related to the survival of a dirigist and state-control mindset from the Ujamaa period, which still plays a large role in political thinking, if not rhetorically, then in practice. Cooksey (2011b) argues that there is "a 'control mentality' among government officials, lack of empathy for business needs,

deficiencies in the legal system and pervasive corruption". Third, as seen with the failed attempt to harvest the low hanging fruits in improving the business environment, bureaucratic infighting and factionalism have undermined the implementation of policies adopted by the government. Based on the weak capacity of the Tanzanian government to promote industrialization effectively over the decades, it can be questioned whether the government has the ability to oversee the development of the extractive sector to the benefit of Tanzanian industrial development.

4.1.7 Summary

In response to the structural adjustment programmes of the 1980s and 1990s, Tanzania adopted a relatively liberal approach to foreign direct investment in extractives. While Tanzanian mining legislation set out ambitions regarding local linkages and ownership, there were no mandatory requirements. Moreover, tariff policies and tax exemptions for foreign firms undermined efforts to increase local content. The liberal approach to mining management has drawn widespread criticism, and since the second half of the 2000s, Tanzania has become more assertive in relation to foreign investors. The linkage opportunities related to new discoveries of gas risk becoming embroiled in a highly politicized debate that is shaped and informed by more or less valid interpretations of previous experiences of the gold industry.

4.2 MNC influences on linkage formation

The scope and depth of linkages are also shaped by the policies and strategies of MNCs. Generally, MNCs are poised between incentives for internalization and incentives

for outsourcing, the current trend being toward the outsourcing of non-core activities in order to increase efficiency, reduce costs, diversify risks and acquire access to capabilities (Doh, 2005; Sako, 2006). This tendency is also evident in the natural resource extraction industry (Morris et al, 2011a), where a massive reconfiguration of lead firms' value chains has taken place in recent years so that such firms are increasingly becoming overseers of complex webs of supplier and service providers collectively contributing to the resource extraction process. Obviously, as outsourcing to a third party may incur transaction-related costs and risks (e.g. compromising reputation, disruption of supply chains, leakage of technology, etc. (Hennart, 1982)), there are limits to the extent to which MNCs will outsource activities.

Hence, at the most general level, the extent of linkage formation in extractives is a result of lead MNCs' outsourcing strategies. But at the operational level, linkage formation is a result of concrete sourcing and procurement strategies and programmes adopted by MNCs. Outsourcing is typically a carefully planned and strategic process, with significant resources being invested in identifying, negotiating with, training and upgrading prospective suppliers and service providers. In the Tanzanian case, we can identify a number of such specific MNC strategies and programmes to foster linkages to local industry, as described in what follows.

4.2.1 MNC strategies and programmes to foster linkages.

Some MNCs are seeking to form linkages, either by adopting local procurement programmes or by seeking to develop the capacity of the local supply industry. Sometimes linkage formation programmes are part of

MNCs' commercial strategies and sometimes they are conceived as an aspect of corporate social responsibility (CSR).

4.2.2 Local procurement and supplier development programmes

The main gold mines have or have had local procurement programmes (Hanlin, 2011). This is confirmed by the case studies conducted for this report. Barrick established a supplier development programme, which implied running workshops in Dar es Salaam where local suppliers were informed about the requirements and procedures for becoming suppliers to Barrick. The Barrick supplier development programme included the mapping of suppliers, vocational training and supplier development. However, after three years the programme was given up, as local suppliers were unable to develop sustainable businesses from the linkages. This was due partly to the high safety and technical standards required by Barrick and partly to the challenging business climate for SMEs in Tanzania.

One MNC currently in the process of developing a major Tanzanian operation within industrial minerals interviewed for this project reported that it does not yet have specific local procurement programmes, though it plans to procure "as much as possible locally". The company is developing a shortlist of prospective local suppliers, here only registered firms with a bank account and at least three quotes from other companies. Working with local suppliers implies a very substantial investment in contract formulation, reviews and safety procedures, and the company predicts that a lot of resources will go into upgrading and policing the suppliers. However, "we don't want to be in the business of development". Hence, the company is adamant

that boundaries between the government and the MNC are clearly drawn with regard to local supplier development: "if government expects more local procurement, they must develop local industry; if they expect more local employees, they must provide vocational training". A factor placing a limit on this company's commitment to local supplier development is that it risks spending large resources on upgrading local supplies which may then be wasted if the investment fails or if the upgraded suppliers find other MNCs to partner up with. In any case, the company does not have high hopes for local procurement in Tanzania. Based on experiences of other gold mines in Tanzania, the company expects "5% of value if we are lucky, depending on how much we can unbundle our contracts to allow local middle men to come in". A particular problem with regard to this "unbundling" is that the operation of the mine will be outsourced. Hence, it will in most cases be the operator who will work with local suppliers. This means that the lead MNC must work through its operator to ensure local sourcing. At some point the company made an attempt to set standards for a contractor firm regarding local hiring, but this led to complaints from the contractor. Of course, the lead MNC could insist on local hiring and local procurement at the contractor firm, "but the problem is that we don't have that specific knowledge about his industry".

Another MNC interviewed for this project was contemplating a large oil and gas investment in Tanzania. As part of the investment, the company would seek to procure as much as possible locally. The company was currently assessing the local supply capacity, dividing suppliers into three groups: those that can serve as suppliers right away, those that need significant upgrading, and those

that can only become suppliers in the long term. While the company has the objective of procuring as much as possibly locally, under no circumstances will it compromise safety and health standards. It is admitted that this policy seriously limits the field of potential local suppliers. As the company expects to be in Tanzania for the long haul and knows that documented contribution to the country's development agenda is key to its 'license to operate', it has engaged itself strongly in local capacity development, for example, by supporting education and vocational training activities related to the oil and gas industry, and more broadly, by facilitating clustering between potential supplier firms.

From the above rather scattered evidence, it seems clear that some MNCs are working with local procurement and supply chain development. Hence, we find evidence of supplier screening, training and monitoring. However, most of the evidence is related to future investments in industrial extractives and gas, and especially in the "old generation" extractive investments, it appears that local supplier development has taken root only recently. Indeed, based on his review of the gold mining industry in Tanzania, Mjimba (2011: 4) concludes that "beyond a general commitment to local sourcing, at a micro-level the buying firms have no effective policies to develop and utilize local linkages and are not actively developing local capacity. The firms are taking advantage of liberal trade policies that permit unrestricted importation of goods and services destined for the sector".

While a lack of "effective policies" among MNCs may explain weak supplier development and linkage formation in Tanzanian gold, our interviews also pointed toward some highly tangible practical barriers to linkage formation. First, MNCs cannot compro-

mise standards related to quality and especially safety. Due to the inability of Tanzanian suppliers to meet such standards, local supplies will typically be confined to non-complex and low criticality inputs. Second, decisions about standards for inputs are typically taken at the headquarters of the MNCs and not locally. As large MNCs are increasingly streamlining and standardizing their procurement programmes and standards globally in order to obtain global scale advantages and global synergies, they are reluctant to develop location-specific standards and requirements that could open up entry to local suppliers (Hanlin, 2011; Morris et al, 2011a). Third, the transient nature of the expatriate workforce (typically expat technicians and managers operate in eight-week shifts) makes it difficult to build long-term and sustainable contacts with local industry. Finally, as mentioned by one of our corporate informants, lead extractive MNCs will typically deal only indirectly with local suppliers, as most of their turnover is procured from preferred global suppliers and contractors. Consequently, the main work in developing local suppliers will have to be undertaken by foreign suppliers and contractors rather than the lead extractive firms, creating numerous principal-agent problems in terms of implementing local content.

4.2.3 CSR and local community development

Local procurement and supplier development activities are not only part of MNCs' quest for efficiency, cost reductions and risk diversification. They are also part of the corporate social responsibility (CSR) programmes that today are adopted by most large MNCs. As part of such programmes, MNCs may foster linkages with local communities.

The literature provides a number of examples of MNCs working with local commu-

nities. As Cooksey reports (2011), between 1999 and 2004 the mining industry spent approximately USD 12 million on education projects, health projects, and water projects, with the latter accounting for more than half. Kweka (2009) reports that Africa Mashariki Gold Mines has made investments in excess of USD 1.5 million in local infrastructure development, including investments in health services, education, water and roads. Kweka (2009) estimated that by 2008 mining MNCs had invested approximately USD 35 million in local community development activities, concluding that, although these investments seem small in relation to total mining investments, they are important to poverty alleviation policies at the local level. Ledesma (2013), in a study of the Tanzanian and Mozambiquan gas industry, reports that companies that are investing in the natural gas sector in Tanzania are undertaking community development programmes and are promoting public-private partnerships in order to be allowed to undertake investments. Several of the mining MNCs operating in Tanzania (as well as the Tanzanian government) are subscribers to the EITI (Extractive Industries Transparency Initiative), which obliges suppliers to maintain transparency and openness with regard to the revenues from extractives.

CSR activities are also reflected in our case studies, where we find that both Barrick and Tanzanite have local community development programmes related to the construction of hospitals and schools, the sponsorship of tertiary education and the provision of local infrastructure, such as water provision and road construction. One of our corporate informants reported that it has a local community development programme, but also that it is essential to explain to local communities that there are limits to how much the mine can do. For this informant, local communi-

ty management is very much a question of adjusting expectations, explaining where the money is going and what local communities can expect from the mine.

While CSR may be viewed as a non-commercial activity by some MNCs, other MNCs have a more strategic view of CSR and local community development. One of our corporate informants argued that “the better local relations, the more security”. Thus, in such MNCs local community and CSR programmes are viewed as a “license to operate” and as a risk management tool (Hanlin, 2011). Especially in mining, local procurement and local job creation are often necessary to maintain stable relations with local communities. This is not least because mines may be located on communal land, may have severe local environmental consequences and/or may infringe on the activities of artisanal miners (Cooksey, 2011a). Indeed, the business organization BSR (Hackenbruch and Pluess, 2011) reports that non-technical risks related to local community relations, rather than technical and commercial risks, might be the greatest risk factor that MNC extractive firms face in Tanzania.

4.2.4 The costs of local content seen from an MNC perspective

Several corporate informants are concerned that linkage activities may add significantly to their costs and eventually render investments less profitable. Barrick reports that the cost levels of Tanzanian gold mining are among the highest in the world (<http://www.barrick.com/investors/quarterly-reports/default.aspx>). Together with other government-induced costs (taxation, royalties and costs of compliance with local standards for environment, health and safety), requirements for local content may significantly affect the net present value (NPV) calculation of the mining inves-

tor. While it is difficult to find evidence that investors have foregone investments in Tanzania due to actual or expected local content requirements, Cooksey (2011) suggests that a generally worsening mining investment climate in Tanzania has contributed to gold mine investors withdrawing investment (Cooksey, 2011a).

4.2.5 Summary

Overall, several extractive MNCs seem to have been trying to find ways in which they can work with local linkage formation, either as part of their commercial and risk management strategies, or as part of their CSR strategies. Based on our admittedly scattered case studies, it appears that the ‘new’ investors in gas and other industrial use extractives are highly focused on developing local content, whereas the ‘old’ investors in gold and other precious minerals seem to have less elaborate local content activities. These apparent industry differences could partly be related to different best local content practices in different industries and partly to the timing of the investments. Hence, the gold mines entered Tanzania at a point of economic development when very few local industries were able to work with MNCs, when local regulatory capacity was exceptionally weak and when the overall investment regime was very liberal. For the ‘new’ generation of extractive investors, the pressures and incentives related to local content may be fundamentally different.

4.3 Local industry influences on linkage formation

The formation of linkages and learning from linkages require that there are local firms with some level of capacity to work with MNC

buyers. One of the main obstacles to linkage formation in Tanzania is related to the weak capacity of Tanzanian manufacturing, as described in what follows.

4.3.1 The manufacturing problem of Tanzania

The reforms of the 1980s and especially the privatization of the approximately 400 state-owned enterprises during the 1990s were driven by donor pressures rather than “pragmatic considerations about future industrial policy” (Therkildsen and Bourgoignie, 2012). Eventually these efforts led to a virtual ‘de-industrialization’ of Tanzania (Arkadie and Dinh, 2004). It seems that Tanzanian manufacturing industry never fully recovered from that shock.

There is little doubt that Tanzanian manufacturing development is lagging behind in terms of the quantity and quality of industrial goods produced (UNIDO, 2012), and in a de-industrializing continent, Tanzania has been a frontrunner. According to UNIDO (2012), the manufacturing sector’s share of GDP stagnated at around 9-10% between 2000 and 2010. This places Tanzania below the African average (which is low) and as one of the least industrialized countries in the world. UNIDO (2012: 35) concludes that manufacturing industries are only in their infancy in Tanzania and that the value addition process in manufacturing is dominated by “low processing of resource-based products – when this is taken into account, the real level of manufacturing decreases even further”. A 2008 Industrial Survey identified a mere 680 manufacturing companies with more than ten employees in Tanzania. The few large Tanzanian companies had in most cases foreign ownership, and companies with foreign ownership accounted for 60% of manufacturing employment (Therkildsen and Bourgoignie, 2012).

Local industry can essentially be divided into the large incumbent firms that control most of Tanzanian industry, the entrepreneurial newcomers (typically SMEs) and the huge number of small and micro enterprises in the informal sector (UNIDO, 2012). The incumbents are typically large industrial conglomerates such as Bakhresa Group and Mohamed enterprises, often controlled by Tanzanians of Indian or Arabic origin. These conglomerates are dominating industries such as trade, transport, telecommunications, construction, tourism and media and are often spin offs from trading companies (Sutton, 2012). Sometimes they embark on internationalization into regional markets with similar market structures, such as Uganda or Rwanda. Incumbents are often incentive- and policy-driven, owing their businesses to concessions, rights, titles and exemptions granted by the government. As a consequence, they tend to see the openness and inflow of FDI as a threat to their incumbent positions, which they will protect by advocating selective tariff policies. While in theory these conglomerates have the capacity to develop viable supplier firms that can link up with extractive MNCs, their shelter mentality may prevent this from happening.

The SME segment could potentially form the basis for the development of a viable Tanzanian supplier industry within extractives. However, the SME segment is weakly developed in Tanzania. Hence, Tanzania clearly displays the ‘missing middle’ characteristics that are also known from other African countries, with a noticeable lack of SMEs in the industrial structure. The weak position of SMEs is to a large extent the result of the very difficult business environment in Tanzania described previously in this report, an environment which favors large firms and discourages firms from moving out of informality (World Bank 2008b;

Cooksey, 2011). For newcomer SMEs, it is very difficult to break into the privileged positions occupied by the Tanzanian conglomerates. One consequence of the underdeveloped SME sector is that the dynamism in Tanzanian industry becomes limited: according to UNIDO (2012), only 11% of formal industrial employment in Tanzania is generated in firms created after 2004.

4.3.2 Technology gap

Apart from the fact that there are few local manufacturing and service firms that can or will link up with foreign investors, the technology gap between MNCs and local industry generally appears to be too large to bridge. Several studies suggest that the technology gap and low absorptive capacity seriously undermine attempts to promote developmental linkages. A 2003 cross-sectoral study found that backward linkages were limited due to low absorptive capacity in Tanzania (Portelli and Narula, 2006). Similarly, a 2011 UNIDO survey of the availability of skills in Tanzanian manufacturing found that two thirds of high-skilled companies reported that it was ‘not easy’ to find a suitable workforce. In a cross-sectional survey of Tanzanian firms, Diyamett et al. (2011) found that local firms have limited linkages with MNCs and that they were rarely able to learn from them: only about 16% of local firms acquired product technological capabilities from MNEs, while about 84% acquired them from other sources, and only about 13% of local firms acquired process technological capabilities from MNEs.

4.3.3 Summary

The weak link in the efforts to create local linkages in extractives is the capacity of Tan-

zaniaan industry. Tanzania has witnessed a virtual deindustrialization in recent decades, and the capacity of local industry to link up with foreign MNCs is highly limited. The further development of effective local supply industries is hampered by a deficient business environment and by the dominance of local conglomerates that have little interest in developing linkages with foreign firms.

4.4 Donor influences on linkage formation

Donors play an important role in Tanzania and are involved at almost all levels of government. Some even argue that donors are the most important player in policy and its implementation (Hyden, 2005; Mmuya and Tostesen, 2007). However, others (e.g. Lawson and Rakner, 2005), argue that “in practice it is domestic political factors which exert a dominant influence over policy” and that donor influence, while often deeply resented, is merely “tolerated” (Therkildsen and Bourguoin, 2012). Regardless, donors are important players in Tanzania.

4.4.1 The new challenge for donors posed by extractives

As natural resource extraction may dramatically alter the Tanzanian government’s revenues – as already mentioned, the newly discovered gas fields could provide as much as 40% of current revenues – donors need to take an interest in the sector. 30-40% of the Tanzanian state budget is funded by donors, and donors are increasingly allocating assistance as general and sector budget support. The expected natural resource revenues may reduce the need for budget support. Moreover, these revenues may accentuate the problem of the *fungibility* of aid money, that is, the problem that development assistance

may indirectly be funding other sectors of the economy than those intended through the aid. Related to this, there is a risk of *moral hazard*, where the Tanzanian government may fail to scrutinize its tax base effectively due to the discretionary funds obtained from donors and natural resource revenues. For these reasons, donors are pushing for greater transparency in the collection and allocation of natural resource revenues.

While donor support has traditionally focused on poverty alleviation, health and education as well as agricultural development, a growing focus has more recently been directed toward private-sector development assistance. Several of the private-sector development activities adopted by donors are directly or indirectly relevant to linkage formation in extractives. For instance, donors (e.g. DFID, USAID, SIDA and Danida) have invested heavily in improving the business environment, thus promoting better conditions for contract-based business collaboration, including those related to MNC–local firm linkages. The Private Sector Support Program (PSSP) from 2006, established by the UNDP, UNIDO and ILO, specifically aimed to bridge the capacity gap faced by local suppliers. Donors have also invested in developing clusters (e.g. the SIDA-funded Cluster Initiative Project) to compensate for some of the competitive disadvantages of local supplier firms in Tanzania. Finally, donors have recently adopted various value-chain approaches to private-sector development; according to an estimate by one embassy, 64 donor-supported value chains are in progress in areas such as corn, sunflower, wheat, etc.

4.4.2 Donor activities in extractives

Some of these donor activities are directly targeted developments of the natural re-

source extraction sector. As mentioned, since the early 1990s the World Bank has been very active in promoting liberalization of the mining sector and has invested heavily in modernizing Tanzanian mining management. By 2013, it seemed that donors, led by the World Bank, were re-positioning themselves on the issue, now in relation to the expected surge in gas FDI. On the one hand, there were efforts to introduce some level of coordination in relation to natural resources. There were, for instance, regular lunch meetings between like-minded donors, including the UK, Brazil, the UAE, the World Bank, ADB, the EU, Holland, the UK, Norway, Sweden and the US. On the other hand, there was also intense competition as donors sought to become the preferred partners in the expected take off of Tanzanian natural resources. Hence, several donors undertook scoping missions and analyses related to extractives: joint studies were underway by DFID and the World Bank on training and on tertiary education; the Netherlands Government focused on primary and secondary education activities related to extractives, SIDA and CIDA focused on fiscal and institutional issues; NORAD had already been strongly involved for several years in technical assistance to revenue management in Tanzania and supported scholarships and faculty exchange related to natural resource extraction capacity building.

If we look at donor involvement in linkage promotion specifically, it is evident that hitherto donors have not been strongly involved. One reason is that linkage promotion has in many ways been contrary to the liberalization agenda that motivated much donor intervention in Tanzania in the 1990s and 2000s. Thus, donors have problems in coming to grips with the more interventionist agenda inherent in linkage formation. Moreover, the link between linkage formation and poverty

alleviation is indirect at best, and donors are struggling to make the link both conceptually and practically. In spite of these challenges, it appears that donors are gearing up for linkages and local sourcing. For instance, the World Bank is scoping for studies in the gas field, exploring how the opportunities offered by gas can be leveraged by increasing local context in a realistic way. Together with DFID, the World Bank put out two tenders in the area, one on local suppliers in mining and one on local mining mainstreaming. The USD 2 million studies include a gap analysis identifying the inputs and quality needed, the demand expected and the potential supply. The World Bank also engaged in the dissemination of best practices and, together with the IFC Advisory Services, it collected and consolidated experiences from various natural resource-dependent countries in order to identify best practices regarding local content and supplier development.

Donors are aware of the huge risks of rent-seeking and corruption in linkage formation and are therefore seeking ways to ensure transparency and reliability in linkage formation, an effort that is parallel to the transparency initiatives related to revenue collection. Ledesma (2013) proposes that donors should ensure that all contracts, project selection and payments are monitored and audited by an independent body and disseminated to the public. Moreover, it is suggested that Tanzania should be assisted in building institutional capacity to monitor progress on the implementation of supplier development and local procurement programmes and to develop common methodologies for measuring indirect effects such as job creation.

The linkage activities of donors are closely related to other areas of donor intervention. On the one hand, linkage policies may

affect the effectiveness of other areas of intervention. Negatively, large demand in extractive-related industries may crowd out jobs and investments in other sectors. Positively, it may generate spillovers by generating new competences and activities in industries unrelated to extractives. On the other hand, linkage promotion requires coordination with other areas of intervention to be effective, e.g. tariff policies, private-sector development policies, FDI policies etc. At the most generic level, linkage activities, to be effective, need to be part of the general industrial development policy framework (Tordo et al., 2013).

4.4.3 The politics of donor intervention

There are several concerns on the part of the Tanzanian government with regard to intervention by donors in extractives. First, the government appears to have a rather strained relationship with its multilateral donors in the field of extractives. This is mainly due to the perceived overzealous liberalization policies of the 1980s and 1990s, which, according to many Tanzanian observers, were imposed by the World Bank and IMF and allegedly led to missed development opportunities. Second, as several of the donor countries have large economic interests at stake in developing the Tanzanian natural resource sector, there are concerns that donor intervention will become an instrument of national economic interests and that donors will coordinate with private business. Cooksey (2011) reports that over the years, whenever disputes over mining have arisen, bilateral donors have lobbied and intervened on behalf of their national firms. These concerns, of course, mainly relate to donor countries like Canada, the US, the UK, Norway, Australia and not least China, which all have major mining interests in

Tanzania. But also other donor countries that at first sight are not involved in natural resource extraction may have substantial commercial interests in the field, mainly through major first-tier supplies. While donors report that they are trying to erect watertight barriers between the commercial interests of individual companies and aid activities in this field, there will always be a suspicion of 'hidden agendas'.

The donor landscape in the field is further complicated by the fact that donors that are less concerned with conflating commercial and aid interests are lurking in the corridors. Hence, the Chinese seem less afraid of combining financial and infrastructure support with extractive foreign direct investments. Indeed, the fact that Chinese investments in extractives can be accompanied by additional investments in infrastructure and education may give Chinese investors an edge over western investors (Alden and Davies, 2006; Luo et al., 2010). The Chinese presence in Tanzania's extractives has been limited until recently, but this may soon change: in 2011 China's Sichuan Hongda Co. Ltd. committed USD 3 billion to coal and iron mining in the Mchuchuma region, and in the spring of 2013 the Chinese president visited Tanzania. During his visit, no less than seventeen memorandums of understanding (MOUs) were signed, including MOUs related to extractive development. For instance, the Chinese pledged support for the development of the harbor in Tanga and agreed to provide finance for the pipeline that will bring gas from southern Tanzania to Dar es Salaam.

4.4.4 Summary

Overall we find that donors have played an important role in developing Tanzania's

natural resource management, though also that they now are facing a new situation in which the Tanzanian government has a much stronger bargaining position due to the arrival of new donors and the expected huge revenues from extractives. Moreover, donors are struggling to formulate a new extractive agenda that goes beyond the open door, liberal approach that characterized earlier donor intervention in the sector.

5. DISCUSSION AND CONCLUSION

Tanzania has been singularly unsuccessful in its attempts to foster linkages between foreign firms and local industry. While the growing FDI inflows may have offered many benefits to Tanzanian development in terms of job creation, exports and technology transfer, it is broadly understood that Tanzania has not been able to reap the full potential of these investments. The largest FDI sector is mining, in particular gold mining. Generally, these investments have failed to produce broad and deep local horizontal and vertical linkages. In their pursuit of greater efficiency, reduced costs, risk diversification and asset augmentation, MNCs are indeed fostering many linkages with supplier and service providers, though these are mainly foreign firms. Hence, the high standards required by lead-mining MNCs provide prohibitive entry barriers for a local industry that rarely has the capacity or the strategic vision to contract with extractive MNCs. At the end of the day, linkages in Tanzanian extractives remain weak and shallow.

Tanzania's past experiences with extractive FDI mainly in gold have informed the current debates on extractives management and

potentially created a rather adversarial political environment for the upcoming generation of extractive investors. However, it is essential to keep in mind that the experience of gold mining cannot necessarily be extended to other extractive industries. Arguably, the linkage potential in gold is limited due to the historically (but not in recent years) weak financial position of this industry, its limited integration into global value chains and the relatively unsophisticated nature of its technology. With the advent of industrial extractive FDI in Tanzania, this rather bleak picture may change. Lead MNCs in oil and gas, nickel, coal, uranium etc. appear to have more advanced local supplier development and CSR programmes than gold mining and thus hold greater linkage potential. The potential of linkages in these new extractive industries goes beyond the immediate local supplier firms. Hence, the development of supply industries can be a catalyzer for development of the Tanzanian manufacturing sector more generally as MNC suppliers become centers of excellence in the local industry, setting new standards for other firms and producing spillovers through competition, demonstration and the migration of talent.

A clear point of contention with regard to future linkage formation in Tanzania is whether linkages are formed more or less automatically as part of MNCs' and local firms' pursuit of efficiency and risk diversification, or whether there need to be clear government-imposed regulation and incentives in place. On the one hand, the liberal position, as laid out in the World Bank's 1992 paper on extractives (World Bank, 1992), holds that open-door policies with the liberalization of investment regimes and across the board policies to strengthen the business environment and improve infrastructure would lead to the formation of linkages. The reason

why linkages evidently have not succeeded in Tanzania according to this view is mainly that infrastructure, the investment climate and institutions are all underdeveloped, that the local supply industry is feeble or non-existent and that misguided regulations have provided disincentives for local linkage formation. Remedies to these problems would include greater transparency in regulation, liberalization of the local private sector, better institutions and infrastructure, and good governance. On the other hand, the interventionist position argues that, left to themselves, market forces will produce few and mostly symbolic linkages. Hence, selective and targeted policies are required if linkages are to be formed. This could, for instance, involve screening investors with high linkage potential, formulating clear requirements and standards for local content and procurement, or mandating local ownership. By formulating local content and other requirements to linkage formation, the Tanzanian government can, according to this view, ensure that extractive MNCs' sourcing strategies become aligned with national development objectives. Extractive FDI will not only lead to the development of a local supplier industry related to extractives, it may also, through spillovers, lead to the development of other industries.

It is our view that Tanzania will be better served by abandoning the highly liberal approach to FDI that has characterized Tanzanian extractive management during the last two decades. This approach may have been right in a situation where the objective was to (re-)build the extractive sector and attract foreign investors to assist in this process. Now Tanzania holds stronger cards and can focus more on spurring the broader development effects of extractive FDI. Indeed, our analysis showed that, after two decades

of World Bank-sponsored liberal policies where the focus has been on developing the general business environment according to the Doing Business regime and/or creating greater transparency, the Tanzanian government now is contemplating a more interventionist approach. Hence, Tanzania seems determined to include local content requirements and other linkage-promoting measures in upcoming legislation on gas, mining and land. We agree that Tanzania should seize the development opportunity offered by the surge in extractive FDI by adopting more interventionist approaches. First, it should formulate a clear strategy as to how extractive FDI can contribute to industrial development in Tanzania that can focus the efforts of different ministries and administrative levels. Hence, as our analysis has demonstrated, the lack of coordination between ministries and bureaucratic infighting may have hampered the development of the extractive sector, including attempts to foster local linkages. Second, Tanzania should screen MNCs more actively for their linkage potential before approving investment projects. Hence, as we have also demonstrated, there are large variations in the degrees to which MNCs work with local linkages through local procurement and CSR programmes. Tanzania needs to focus its efforts on those firms with large documented linkage potential. Third, as one of the main obstacles to linkages is, as our analysis clearly demonstrated, the weak capacity of Tanzanian supply industries, it is paramount that the Tanzanian government adopts targeted measures to develop the capacity of local supply industries, for example, through dedicated training, cluster programmes and tax incentives. Fourth, the Tanzanian government should actively encourage MNCs to engage in linkage formation and local sup-

plier development, preferably through voluntary measures, but possibly also through mandatory measures, as long as such measures are realistic and phased in in a gradual manner.

It is clear that the proposal we have outlined is largely in line with the interventionist approach depicted above. But we also believe – and here we are more in line with the liberal approach – that linkage-promotion policies should be implemented in a context with functioning market-support institutions, and that this should take into account the governance capacity of the Tanzanian government. First, our analysis clearly suggested that one of the largest barriers to linkage formation in Tanzania is related to the toxic business environment, which makes it more than difficult for qualified local supplier firms to evolve and which poisons contract-based business relations, that is, linkages. In fact, while a difficult business environment may be manageable for large extractive MNCs, it may not be for local supplier firms; in that sense, the lack of linkage formation may be the ultimate price paid for a weak business environment. Thus, we argue that improvements to the Tanzanian business environment must go hand in hand with any attempt to introduce more targeted linkage-promotion policies. Second, while in theory assertive linkage policies may be desirable for Tanzania, it would be naïve to ignore the limited governance capacity of the Tanzanian government to implement such policies. While the Tanzanian government has no doubt been strong in the sense that it has been able to deliver political stability over a long period of time, it has a weak track record in terms of pushing institutional reform and industrial development. In such a weak governance and institutional context, linkage policies may easily become

embroiled in ministerial infighting, captured by rent-seeking bureaucrats and politicians, and/or distorted by entrenched business interests. Therefore, it is essential that linkage promotion adjusts its level of ambition to the actual executive power of government and minimizes opportunities for distortions, rent-seeking and capture. This means introducing linkage measures gradually and cautiously and above all ensuring openness and transparency in linkage formation.

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