THE LANDSCAPE FOR IMPACT INVESTING IN EAST AFRICA
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We would especially like to thank our interview participants—without their key insights this report would not have been possible. We include a full list of interviewees in the Appendix.

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AUGUST 2015
<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
</tr>
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<tbody>
<tr>
<td>AFD</td>
<td>Agence Française de Développement (French Development Agency)</td>
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<td>AfDB</td>
<td>African Development Bank</td>
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<tr>
<td>BIF</td>
<td>Burundian Franc</td>
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<tr>
<td>BIO</td>
<td>Belgian Investment Company for Developing Countries</td>
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<tr>
<td>BoP</td>
<td>Base of the Pyramid</td>
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<tr>
<td>CEPGL</td>
<td>Communauté Économique des Pays des Grand Lacs (Economic Community of the Great Lakes Countries)</td>
</tr>
<tr>
<td>COMESA</td>
<td>The Common Market for Eastern and Southern Africa</td>
</tr>
<tr>
<td>CSR</td>
<td>Corporate Social Responsibility</td>
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<tr>
<td>DFI</td>
<td>Development Finance Institution</td>
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<td>DFID</td>
<td>The Department for International Development (United Kingdom)</td>
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<tr>
<td>DRC</td>
<td>Democratic Republic of the Congo</td>
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<tr>
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<td>East African Community</td>
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<tr>
<td>Early-stage business</td>
<td>Business that has begun operations but has most likely not begun commercial manufacture and sales</td>
</tr>
<tr>
<td>EIB</td>
<td>European Investment Bank</td>
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<tr>
<td>ESG</td>
<td>Environmental, Social, and Governance</td>
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<td>ETB</td>
<td>Ethiopian Birr</td>
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<td>FDI</td>
<td>Foreign Direct Investment</td>
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<tr>
<td>FMCG</td>
<td>Fast-Moving Consumer Goods</td>
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<tr>
<td>FMO</td>
<td>Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V. (Netherlands Development Finance Company)</td>
</tr>
<tr>
<td>Focus countries</td>
<td>Countries under the study where non-DFI impact investors are most active in. Namely Ethiopia, Kenya, Rwanda, Tanzania, and Uganda</td>
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<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>GEMS</td>
<td>Growth Enterprise Market Segment</td>
</tr>
<tr>
<td>GIIRS</td>
<td>Global Impact Investing Ratings System</td>
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<tr>
<td>GIZ</td>
<td>Gesellschaft für Internationale Zusammenarbeit (German Agency for International Cooperation)</td>
</tr>
<tr>
<td>Growth-stage business</td>
<td>Company has a functioning business model and its current focus is developing new products / services or expanding into new markets</td>
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<tr>
<td>HDI</td>
<td>Human Development Index</td>
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<tr>
<td>ICC</td>
<td>International Criminal Court</td>
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<tr>
<td>ICT</td>
<td>Information and Communication Technology</td>
</tr>
<tr>
<td>IFAD</td>
<td>International Fund for Agricultural Development</td>
</tr>
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<td>International Finance Corporation</td>
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<td>International Monetary Fund</td>
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<td>IRIS</td>
<td>Impact Investing and Reporting Standards</td>
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<td>KES</td>
<td>Kenyan Shilling</td>
</tr>
<tr>
<td>LP</td>
<td>Limited Partner</td>
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<tr>
<td>Mature business</td>
<td>Profitable company with a developed and recognizable brand</td>
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<td>MDG</td>
<td>Millennium Development Goal</td>
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<tr>
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<td>Microfinance Institution</td>
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<td>Micro, Small and Medium Enterprise</td>
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<td>Non-Governmental Organization</td>
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<td>Non-focus countries</td>
<td>Countries covered in the study but have limited non-DFI impact investor activity. Namely Burundi, Djibouti, Eritrea, Somalia, South Sudan, and Sudan</td>
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<tr>
<td>OFID</td>
<td>OPEC Fund for International Development</td>
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<td>OPIC</td>
<td>Overseas Private Investment Corporation</td>
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<tr>
<td>PE</td>
<td>Private Equity</td>
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<td>PPA</td>
<td>Power Purchasing Agreement</td>
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<td>PPP</td>
<td>Purchasing Power Parity</td>
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<tr>
<td>PPP</td>
<td>Public-Private Partnership</td>
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<td>PTA</td>
<td>Preferential Trade Area Bank</td>
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<tr>
<td>RDB</td>
<td>Rwanda Development Board</td>
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<tr>
<td>RFP</td>
<td>Request for Proposal</td>
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<tr>
<td>RWF</td>
<td>Rwandan Franc</td>
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<tr>
<td>SACC0</td>
<td>Savings and Credit Co-operative</td>
</tr>
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<td>SAGCOT</td>
<td>Southern Agricultural Corridor of Tanzania</td>
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<td>SDG</td>
<td>Sudanese Pound</td>
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<td>SGB</td>
<td>Small and Growing Business</td>
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<td>Small and Medium-Sized Enterprises</td>
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<td>State-Owned Enterprises</td>
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<td>SOS</td>
<td>Somali Shilling</td>
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<tr>
<td>SSP</td>
<td>South Sudanese Pound</td>
</tr>
<tr>
<td>TA</td>
<td>Technical Assistance</td>
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<td>Tanzania Investment Centre</td>
</tr>
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<td>TZS</td>
<td>Tanzanian Shilling</td>
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<tr>
<td>UGX</td>
<td>Ugandan Shilling</td>
</tr>
<tr>
<td>UN DESA</td>
<td>United Nations - Department of Economic and Social Affairs</td>
</tr>
<tr>
<td>UNCTAD</td>
<td>United Nation’s Conference on Trade and Development</td>
</tr>
<tr>
<td>USAID</td>
<td>The United States Agency for International Development</td>
</tr>
<tr>
<td>VAT</td>
<td>Value-Added Tax</td>
</tr>
<tr>
<td>VC</td>
<td>Venture Capital</td>
</tr>
<tr>
<td>Venture-stage business</td>
<td>Sales have begun but cannot sustain the company’s operations. The business model is still being aligned with the realities on the ground</td>
</tr>
<tr>
<td>WASH</td>
<td>Water, Sanitation, and Hygiene</td>
</tr>
<tr>
<td>WHO</td>
<td>World Health Organization</td>
</tr>
</tbody>
</table>
TANZANIA
INCREASINGLY POPULAR DESTINATION FOR IMPACT CAPITAL
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INTRODUCTION

Tanzania is a core part of the East African impact investing landscape, and most impact investors active in East Africa operate in Tanzania. Although Kenya remains the primary target for impact capital, Tanzania is an increasingly popular destination.

Despite positive trends, many adverse conditions persist in Tanzania. Sourcing talent, particularly for middle management, remains extremely difficult. Many businesses operate informally with multiple sets of accounts, which can compromise impact investors’ ability to place capital. There are few investment-ready businesses, due in part to the lack of high-quality pre-investment support for promising enterprises. In addition, the nature and timing of government involvement in the private sector is unpredictable and can have severe economic consequences.

Nevertheless, Tanzania has a growing economy and is an area of focus for impact investors. Most impact investors active in the region work in Tanzania, and it has the third largest number of impact investments in East Africa. Moreover, as impact investors diversify beyond Kenya, Tanzania will be a primary beneficiary, and the amount of capital deployed is expected to increase accordingly.

FIGURE 1: MAP OF TANZANIA
COUNTRY CONTEXT

Tanzania is one of the most politically stable countries in East Africa and has seen strong growth in recent years. This is reflected across economic indicators, though the country requires support to improve human development indicators and increase linkages between disadvantaged populations and the rapidly growing national economy.

Notably, Tanzania is a member of both the East African Community (EAC) and the Southern African Development Community (SADC). This dual membership expands Tanzania’s trade options and has resulted in many South African companies being active in Tanzania, despite them being much less active in other East African countries.

Gross Domestic Product

Tanzania’s GDP has grown approximately 8% year-on-year in PPP terms between 2004 and 2013 (Figure 2). GDP stands at USD 86 billion in PPP terms, though only USD 36 billion in current price terms. With a population slightly larger than Kenya’s (roughly 49 million), Tanzania has a similar GDP in PPP terms, but a much lower GDP in current price terms. This demonstrates the significantly lower price levels for common goods and services in Tanzania compared to Kenya.

FIGURE 2: GDP (PPP), 2004–2013

Source: IMF World Bank Economic Indicators, April 2014
Foreign Direct Investment

Strong GDP growth has been accompanied by even stronger foreign direct investment (FDI) inflows, increasing at nearly 19% year-on-year over the last decade.¹ Tanzania realized more than USD 1.8 billion in FDI inflows in 2013, the second highest FDI inflow in East Africa.² This large and growing FDI is primarily driven by oil and gas exploration, with the mining and quarrying sector accounting for more than 43% of all FDI inflows between 2008 and 2011.³ The primary sources of this FDI have been the United Kingdom, South Africa, and Canada, which together account for more than 70% of all FDI to Tanzania from 2008 to 2011.⁴

![FIGURE 3: FDI FLOWS, 2004–2013](image)

Source: UNCTAD

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² Ibid.


⁴ Ibid.
Inflation and Exchange Rates

Over the past decade, Tanzania has experienced high and volatile local inflation rates reaching as high as 16%. In addition, the Tanzanian Shilling has depreciated by approximately 6% per year against the US dollar since the beginning of 2008, reducing the hard currency value of local currency debt that international investors disburse in Tanzania. For additional information on the impact of exchange rates on debt instruments, see the East Africa regional chapter.

FIGURE 4: INFLATION AND USD/TZS EXCHANGE RATE, 2004-2013

Since 2008, TZ Shilling has weakened ~6% year-on-year against the USD

Source: IMF World Bank Economic Indicators, Oanda Historical Currency Rates
SUPPLY OF IMPACT INVESTING CAPITAL

Tanzania is typically considered the third country of focus for impact investing in the region, after Kenya and Uganda, and will likely see increased activity as impact investors expand their focus beyond Kenya. That said, the gap in impact investing activity between Tanzania and Kenya and Uganda is large. There have been at least 109 non-DFI impact deals in Tanzania, disbursing approximately USD 227 million in capital—roughly half the number of deals and a third of the capital disbursed in Kenya.

There are 129 impact capital vehicles managed by 92 non-DFI impact investors that actively consider Tanzania—nearly as many as consider Kenya. Most of these impact capital vehicles are active across the region, where more than USD 2.5 billion in capital committed regionally could be deployed in Tanzania (Figure 5). Tanzania, however, is likely to capture only a small share of this capital if historical deal flows persist. There is less than USD 35 million that has been committed exclusively to Tanzania. Most of the non-DFI impact investors active in Tanzania focus on early-stage businesses that have some track record and operational structures in place.

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Figure 5: Total Capital Committed by Non-DFI Impact Investors

USD MILLIONS

<table>
<thead>
<tr>
<th></th>
<th>MULTIPLE COUNTRIES, INCLUDING TANZANIA</th>
<th>ONLY TANZANIA</th>
</tr>
</thead>
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<td>USD MILLIONS</td>
<td></td>
<td></td>
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<tr>
<td>3,000</td>
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<tr>
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<td>1,500</td>
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</tbody>
</table>

Source: Open Capital Research

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Due to the unique nature and large size of development finance institutions (DFIs), the authors of this report analyzed their activity separately from those of other types of impact investors (“non-DFI”), and present this separate analysis when appropriate. See the Introduction and Methodology section of this report for more details.
Broader Investing Landscape

Impact investment assets represent a small part of the overall investment picture in the country. For example, local banks had more than USD 11 billion in assets under management in 2011 (Figure 6) while additional sources of capital—such as commercial private equity funds, hedge funds, savings and credit cooperatives (SACCOs), and microfinance institutions (MFIs)—further increase this number. Indeed, banks had more than USD 4.5 billion of outstanding loans in 2011, or nearly 20 times the known disbursements made by non-DFI impact investors in Tanzania to date and more than four times more than known disbursements made by all impact investors in Tanzania.

![Figure 6: Impact Capital Relative to Other Financial Assets](source: Bank of Tanzania, Tanzania Chamber of Commerce, Open Capital Research)

Although impact investing represents a small portion of total investment activity, it fills an important gap in the market for the early-stage businesses of interest to most non-DFI impact investors. Tanzanian banks remain risk averse, even more so than in other East African countries, and are often unwilling to invest in start-up or early-stage enterprises. When willing to lend, they require extremely high collateral ratios, frequently more than 100% of the loan amount.

Entrepreneurs face high interest rates, even if they are able to meet collateral requirements. Over the last ten years, Tanzanian bank rates have fluctuated between 14% and 16%. This compares favorably with Kenya, which has experienced larger volatility and where, as of 2013, rates stood 1.5% higher. Nevertheless, Tanzania’s interest rates remain high by international standards, often more than three times

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7 Ibid.

higher than the average bank interest rate in the United States, which stood below 5% between 2004 and 2013.9

Stringent collateral requirements and high interest rates limit the practical availability of bank financing for enterprises. The limited availability provides a market opportunity for private investors who are able to provide equity and/or debt that is cheaper or has lower collateral requirements.

This gap is at times filled by grants, which are widely available from donors active in Tanzania. Non-DFI impact investors report that they frequently compete with donor funding for high potential deals, as social entrepreneurs speaking with impact investors are often aware of donor opportunities. Even if an entrepreneur is not directly sourcing capital from donors, their presence in the market can complicate negotiations for impact capital as entrepreneurs may view donor funding as an opportunity to raise free capital and to avoid investors’ comparatively high return expectations. Many grant-making institutions, however, are unwilling to lend to commercial enterprises and often have stringent reporting or operational requirements that are less attractive for businesses.

Impact Capital Disbursed

Tanzania boasts one of the most robust deal flows in the region, although it remains well below the level of activity in Kenya. In total, non-DFI impact investors have disbursed at least USD 227 million to date, or about 17% of known non-DFI impact capital disbursed in East Africa (Figure 7). The country has received a similar proportion of known DFI direct investments (about 11%), with nearly USD 850 million disbursed (Figure 7).

![FIGURE 7: IMPACT INVESTMENTS IN TANZANIA](chart)

<table>
<thead>
<tr>
<th>Capital disbursed</th>
<th>Deals</th>
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</thead>
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<tr>
<td><strong>DFI</strong></td>
<td></td>
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<tr>
<td>USD 846 Millions</td>
<td>65</td>
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<tr>
<td><strong>NON-DFI</strong></td>
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<tr>
<td>USD 227 Millions</td>
<td>109</td>
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</table>

Source: Open Capital Research

9 Ibid.
Tanzania boasts significantly more impact investing activity than the next most active country, Ethiopia—about 2.5 times the known amount of non-DFI impact capital disbursed and more than four times the number of known non-DFI impact deals.\textsuperscript{10} This aligns with the view of most non-DFI impact investors that Kenya, Uganda, and Tanzania are the core impact investing markets in East Africa.

**Investments Over Time**

With a large number of deals with undisclosed details, few definitive conclusions can be drawn about the timing of non-DFI impact investing in Tanzania. It is likely that most of these deals occurred after 2010, if consistent with the general trend in impact investing in East Africa.

DFI direct investments in Tanzania have grown over the last four years (Figure 8). The decline for 2014 is likely due to incomplete data at the time of data collection in late 2014, as many attempt to close final investments before the end of the calendar year.

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{figure8.png}
\caption{DFI DIRECT INVESTMENTS BY YEAR}
\end{figure}

Source: Open Capital Research

\textsuperscript{10} Rwanda has more known deals than Ethiopia—38 compared to 25. Tanzania has nearly three times the number of deals as Rwanda.
**Sector**

The distribution of investments by sector broadly reflects impact investor interest. Agriculture and financial services have received the most deals from non-DFI impact investors (over 55%) and have strong interest from several investors (Figure 9). Despite the larger number of deals in agriculture, the large investment sizes possible when placing capital into established banks or MFIs drives a greater total amount of capital to financial services. Similarly, the housing sector has seen significant capital disbursed despite relatively few deals. These projects tend to have larger average deal sizes than other sectors due to substantial construction costs and the frequent need to internally finance mortgages for low-income borrowers. The energy sector in Tanzania has also received significant capital disbursed, driven primarily by three large deals by a single non-DFI impact investor.

![FIGURE 9: NON-DFI IMPACT INVESTMENTS BY SECTOR](image)

Despite their prominence as interest sectors for non-DFI impact investors, education and health have seen relatively few deals. The disconnect between interest in these sectors and the number of deals implies that impact investors see limited viable, investible opportunities and have particular difficulty placing capital.
As can be seen in Figure 10, known DFI direct investments also favor investments in agriculture (20% of deals and approximately 17% of capital disbursed) and financial services (more than 25% of all deals and approximately 16% of all capital disbursed). The energy sector received the most capital (more than 25% of total DFI capital disbursed in Tanzania), although more than half was due to a single large investment.

**FIGURE 10: DFI DIRECT INVESTMENTS BY SECTOR**

![Bar chart showing investments by sector in Tanzania.](chart)

Source: Open Capital Research
Deal Size

As shown in Figure 11, the vast majority of capital disbursed by non-DFI impact investors has been in amounts above USD 1 million, although two-thirds of known impact deals in Tanzania are less than USD 1 million in size. Deals under USD 250,000 represent a full third of all impact deals in Tanzania. These small deals contrast with Kenya, where only about 11% of deals are below USD 250,000, suggesting that non-DFI impact investors are finding that most interesting businesses in Tanzania are still relatively small.

![FIGURE 11: NON-DFI IMPACT INVESTMENTS BY DEAL SIZE](image)

Source: Open Capital Research

By contrast, the average deal size for known DFI direct investments in Tanzania is above USD 13 million (Figure 12), more than six times the average deal size of non-DFI impact investors. This is driven by investments in sizeable energy projects as well as large placements in sectors like energy, extractives, and infrastructure. Even though deals under USD 10 million constitute more than half of the total direct DFI investments, approximately 13% of direct DFI deals were under USD 1 million compared to 67% of non-DFI impact investor deals.

![FIGURE 12: DFI DIRECT INVESTMENTS BY DEAL SIZE](image)

Source: Open Capital Research
Instrument

The large number of deals with undisclosed details prevents a definitive breakdown of non-DFI investment instruments; however, known deals indicate that traditional debt and equity are the most common instruments (Figure 13). Of these known deals, non-DFI impact investors have made nearly twice as many debt investments as equity, aligning with interview findings from investors that it can be challenging to explain equity investments to entrepreneurs. Unlike their counterparts in Kenya or Uganda, non-DFI impact investors in Tanzania reported that they have not begun to use non-traditional structures such as convertible debt or revenue-participating debt.

![FIGURE 13: NON-DFI DIRECT INVESTMENTS BY INSTRUMENT](image)

Source: Open Capital Research

As elsewhere in the region, DFI direct investments are overwhelmingly debt, with a handful of equity deals (Figure 14). Debt investments constitute more than 70% of all capital disbursed and nearly two-thirds of deals made by DFIs directly. Together, debt and equity investments are nearly 90% of direct DFI deals and capital disbursed.

![FIGURE 14: DFI DIRECT INVESTMENTS BY INSTRUMENT](image)

Source: Open Capital Research
Local Presence

A number of impact investors have chosen to place staff on the ground in Tanzania, predominantly in Dar es Salaam, but also in Arusha and Moshi (Figure 15). Indeed, Tanzania is home to more impact capital vehicles than any other country except Kenya, and two impact investors have their headquarters there.

The impact investing community in Tanzania remains small, but because it is dispersed across multiple cities, more businesses have access to a local impact investor. Impact investors interviewed noted that they know each other well and have close, collegial relationships. These connections allow free sharing of information about entrepreneurs and potential investments, which assists investors to develop pipeline and more effectively conduct due diligence on potential investments.

Fluency in Kiswahili is critical to leverage local presence in Tanzania. To a much greater extent than Kenya, Tanzanians do not use English, which can complicate efforts to form relationships. Without Kiswahili, impact investors limit the number of strong relationships they can form and their ability to source new deals.

Impact Tracking Standards

Impact investors’ dual mandate to realize both financial and social returns requires a strong focus on measuring impact as a part of their core activities. Beyond tracking metrics as best practice, many of their supporters require it, including DFIs, which act as anchor investors to most impact funds.

Most impact investors in Tanzania do not specify a standardized approach for measuring the impact of their investments across their portfolio. Instead, they typically use flexible structures adapted to each new investment. Many impact investors have rigorous and rigid impact guidelines to make an investment, but they design and track metrics after the investment in an individualized manner to minimize the burden placed on their portfolio companies. Further information on challenges in impact measurement is provided in the East Africa regional chapter of this report.
DEMAND AND NEED FOR IMPACT INVESTING CAPITAL

There is strong demand for impact capital from entrepreneurs operating in Tanzania. Despite recent progress, there remain significant gaps in the provision of key goods and services, which create opportunities for entrepreneurs to build enterprises that fill key needs while also realizing financial returns.

Development Context

Tanzania has seen recent improvement in human development indicators, but still remains well below global averages (Figure 16). Overall, Tanzania is ranked 159th of 187 countries evaluated in the United Nation’s Human Development Index.11 This low ranking is reflected in poor performance across a number of individual development indicators covering poverty, health, and education.

![Figure 16: UN HDI Scores, 2008-2013](image)


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More than two-thirds of Tanzania’s population, or more than 30 million people, live on less than USD 1.25 per day (Figure 17), nearly three times the global average. This is the second worst poverty level in East Africa, after Burundi.

Tanzania also has poor health indicators, significantly underperforming global averages. Tanzania's under-five and infant mortality rates are both somewhat above global averages.12 Despite being well above global averages, Tanzania’s under-five mortality rate is the second lowest in East Africa, behind only Eritrea’s. By contrast, its rate of under-five stunting, an effective proxy for childhood and later health in general, is slightly worse than the East African average and is more than 50% greater than the global average (Figure 18).13

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**FIGURE 17: POPULATION BELOW USD 1.25/DAY (LATEST AVAILABLE DATA POINT)**

![Population Below USD 1.25/day](source: UN Human Development Report 2014)

**FIGURE 18: UNDER-5 MORTALITY AND STUNTING (LATEST AVAILABLE DATA POINT)**

![Under-5 Mortality and Stunting](source: UN Human Development Report 2014)

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12 Tanzania’s infant mortality rate was 38 per 1,000 live births in 2012, compared to a global average of 34 in 2013. UNICEF Statistics: [http://www.unicef.org/infobycountry/tanzania_statistics.html](http://www.unicef.org/infobycountry/tanzania_statistics.html).

On the other hand, Tanzania’s gross secondary education enrollment is slightly above East African average. Nevertheless, it remains below half of the global average—less than 8% of the Tanzanian population age 25 and above has attended some secondary school, which is less than 15% of the global average (Figure 19).  

FIGURE 19: KEY EDUCATION INDICATORS (LATEST AVAILABLE DATA POINT)

Source: UN Human Development Report 2014

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14 Ibid.
Educational metrics are an especially important indicator for future development given Tanzania’s demographics. Like other East African countries, Tanzania has a disproportionately young population, where nearly 45% is under the age of 15 and more than 60% is below age 25 (Figure 20). This youth boom has led to high unemployment among young people which, when compounded with low levels of education, poses a challenge to economic growth.

![Figure 20: Population by Age and Gender](image)

Source: UN ESA, World Population Prospects

**Entrepreneurs**

As is the case across the region, Tanzania has many early-stage businesses that operate across a range of impactful sectors, including education, housing, healthcare, water and sanitation, energy, etc. These businesses seek capital across the spectrum of funding from start-up and SME-size deals to capital for scaling up, although they are primarily start-up and early-stage businesses. Similarly, non-DFI impact investors focus on early-stage opportunities that have some track record and operational structures in place.

Despite growing interest in placing capital in Tanzania, entrepreneurs face substantial challenges to become investment-ready and struggle to find financing beyond friends and family. Bank financing can be particularly difficult and expensive. As in much of the region, collateral requirements are high. However, this hurdle can be even more restrictive in Tanzania, as impact investors report that banks in Tanzania often do not accept land as collateral because of difficulties arising from community
land ownership. Without land as security, many entrepreneurs, particularly those in agriculture, find it impossible to access bank financing. Non-DFI impact investors note that banks also rarely have products or processes suited to agricultural investments and that they prefer to place capital in government bonds. There have been new entrants to the banking sector from Kenya, but these new banks have yet to significantly expand access to financing.

Impact investors note that many potentially interesting early-stage businesses and even some large businesses operate informally. They often have different sets of accounts for different audiences (e.g., one for the revenue authority, one for their family, and one that is accurate). In such cases, it is difficult for impact investors to build confidence in a business’s operations or trust in the entrepreneur. This makes it hard for investors to disburse capital. Beyond the lack of transparency, informal businesses often do not comply with relevant laws, which is a threshold condition for some impact investors. More generally, informal businesses are significantly less likely to have clear financial records, access to formal markets, or access to government services, making them less likely to be an attractive target for impact capital.

Early-stage businesses face significant challenges arising from Tanzania’s geographic size and poor infrastructure. Low population density implies that growing businesses must expand their geographic reach rapidly, which is challenging. New markets are far from headquarters and must be operated largely as a separate endeavor. For example, inventory, sourcing, and distribution must often be re-created and run independently.

Sourcing adequate human capital to manage these dynamics is one of the most prominent challenges businesses face. As with much of East Africa, there is a limited pool of talented middle and senior management talent and, when available at all, capable managers are costly. This problem is particularly acute in Tanzania because the country does not have a large returning diaspora to supplement in-country talent. Impact investors note that many exciting small businesses have some foreign management, despite many impact investors’ desire to find local entrepreneurs. In some cases, these are managers from the region. Alternatively, some strategic investors have supplied management talent as part of their investment offering. This model overcomes initial management challenges while the fixed timeline requires training of and transition to local management after a short time.

In addition to these challenges, early-stage businesses often suffer from similar challenges as early-stage businesses across the region, such as insufficient human capital and lack of access to bank financing (see the Regional Overview chapter of this report for more detail). Though such challenges are not as common with growth-stage businesses, high potential, rapidly scaling growth companies are significantly rarer. For more detail on the challenges facing both early- and growth-stage companies in East Africa, see the East Africa regional chapter of this report.
ENABLING IMPACT INVESTING: THE ECOSYSTEM

The impact investing ecosystem in Tanzania remains challenging and is a key constraint for investors. Government intervention can be extensive and unpredictable. Impact investors interviewed consider sectors with a history of government involvement broadly unsuitable and report being wary of the government imposing new regulatory burdens on any rapidly growing sectors.

The broader business environment is not yet as developed as it is in other East African countries. There are few active intermediaries or service providers to provide needed pre-investment support and facilitate deal flow. Even though there are a number of accountants and law firms, there is substantial variation in quality. While good advisors are available, they are generally expensive; impact investors estimate legal costs to be twice as high in Tanzania as in Kenya.

Regulatory Environment

Tanzania is one of the most politically stable countries in East Africa and has a generally welcoming regulatory landscape for investors. It is one of the easier countries to conduct business in in East Africa, ranking second in the region in the World Bank’s Ease of Doing Business rankings.\(^\text{15}\) Other than land ownership, there are few differences in regulation for foreign and domestic investors. Investors are able to access foreign currency easily, repatriate profits, and own local companies.

Nonetheless, impact investors report uncertainty around government policies as a major impediment to placing capital. In addition, interacting with the Tanzanian state to pay taxes or apply for licenses can be complicated due to inefficient bureaucracies. Some key features of Tanzania’s regulatory landscape are described below:

- **Repatriation of profits and dividends:** Tanzania does not restrict foreign investors from repatriating returns; profits, dividends, and capital can be easily repatriated after tax.\(^\text{16}\) These repatriations may generally occur in any currency.\(^\text{17}\)

- **Foreign exchange controls:** Tanzania has open foreign exchange rules. Foreign exchange is freely available from commercial banks and can be acquired and held equally by locals and foreign nationals. Any person may open a foreign currency account with an authorized bank. Recently, the Tanzanian government required all


foreign source loans to be registered with the Bank of Tanzania. The reporting obligation lies with the local bank, though individual businesses and impact investors seeking to place capital may be required to share additional information in response to this reporting requirement.

- **Land ownership:** All land in Tanzania is public—the country does not recognize absolute private ownership of land. At most, it may be leased from the government for 99 years. Foreigners are only permitted to lease land through the Tanzania Investment Center (TIC). The TIC has allocated specific plots for foreign investors, although the process to allocate new land can be lengthy. Less than 10% of land has been surveyed and title deed registration is completed manually at the local level, further complicating matters. The TIC maintains a bank of land for investment purposes, but restrictions on foreign land ownership can significantly delay investment.

Foreign investors may form joint ventures with Tanzanians to own land. In these joint ventures, the Tanzanian retains the leasehold and provides use to the foreign investor. In order to be considered a Tanzanian company, a company must be majority owned by Tanzanian citizens.

- **Local ownership requirements:** Foreign investors may purchase up to 100% of any local company except in telecommunications (65% foreign shareholding maximum), shipping (50%), or mining (variable) sectors. Local shareholders are defined as Tanzanian citizens or companies where at least 51% of the shares are held by Tanzanian citizens.

- **Government intervention:** The Tanzanian government remains heavily involved in the economy and can impose difficult regulatory burdens unpredictably. For example, Tanzania has a history of ad hoc decisions to ban exports of certain goods.

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21 Ibid.

22 Ibid.

23 Ibid.

24 Hogan Lovells, *Foreigners’ Land Rights in Tanzania - are they there?* (2014), available at http://www.hoganlovells.com/files/Publication/cf5c8bf2-cc64-46b7-9182-395020bcb732/Presentation/PublicationAttachment/c02e06e1-de0e-4dd5-991b-3cbe3f8f9922/Foreigners_Land_Rights_in_Tanzania_are_they_there_May_2014.pdf.

foods and at one point banned grain exports. The government also sets prices in some sectors, such as coffee and cashew. In some cases, government prices have been set above the international market, meaning local producers are unable to sell through formal channels. Beyond price setting, impact investors believe the government may look to growing sectors for opportunities to raise tax revenue. For example, impact investors expressed concern over a proposal to remove the VAT exception for solar products, but this proposal was later shelved. The government continues to operate state-owned enterprises in large-scale energy, telecommunications, banking, rail, and mining that receive government subsidies and other preferential treatment.


Ecosystem Players

There are a growing number of ecosystem players active in Tanzania. The research team identified 22 active organizations, primarily comprised of consultants and incubators/accelerators. Despite the number of ecosystem players formally active in the market, few impact investors and entrepreneurs interviewed report working with local ecosystem players.

Although there are a number of regional incubators and accelerators, most are based elsewhere in the region. Encouragingly, several new technology hubs have opened in Dar es Salaam. Impact investors think these new hubs are indicative of increasing interest in incubating technology ventures in Tanzania, although they are not able to meet demand today.

These ecosystem players offer similar services as their counterparts across East Africa. As in the rest of the region, the skew towards incubators and accelerators, which tend to focus on seed or very early venture-stage businesses in specific sectors, leaves a gap for service providers to support growth-stage businesses across a range of sectors. For more detail on active players’ service offerings and gaps in the ecosystem, please see the East Africa regional chapter.
Other Ecosystem Players

In line with the general impact investing ecosystem in Tanzania, social enterprises often struggle to access needed services. Every company must produce annual audited accounts and, while there are several high-quality auditors that are well-known in the market, they tend to be prohibitively expensive for small businesses. Outside of these few providers, quality varies widely, as does the reliability of accounts produced. Particularly for small companies, developing clear financial documentation can be challenging, even if they are operating formally.

Legal representation is also available but of varying quality. There are a handful of respected firms that are well suited for high-quality legal due diligence, but they are often too expensive for smaller investments. In general, the lack of broad, high-quality legal representation increases transaction costs for new transactions; impact investors estimate that legal diligence costs in Tanzania are twice as high as in Kenya.
Impact investors based in Tanzania stress that there are many opportunities, but that to be successful, investors need to be flexible in their investment criteria. Rigid criteria around sector, impact, or stage of business can be counterproductive and prevent completing investments. This emphasis on flexibility implies an underlying sentiment that there are still few high-potential entrepreneurs in Tanzania. Without the depth of talent and potential investments present in other countries such as Kenya, there is less room for impact investors to focus only on a sub-set of opportunities.

**Challenges**

There are, however, a variety of challenges for current impact investors, new impact investors, and other eco-system players in Tanzania. Challenges commonly faced in Tanzania include:

- **Insufficient investment-ready deal flow**: As elsewhere in the region, many impact investors struggle to disburse capital in Tanzania. Efforts are complicated by a substantial informal sector where many businesses, even large ones, have multiple sets of accounts. Even if a clear financial history can be determined, informal businesses are seldom fully compliant with applicable regulations. Like companies in the rest of the region, businesses in Tanzania also suffer from inefficient operations, a lack of realistic strategies and projections, and a limited plan to use capital invested.

- **Government intervention**: The government of Tanzania remains actively involved in the economy, and its involvement in specific sectors can be unpredictable. Sudden changes with strong effects on the business environment for a sector are possible and uncertainty about government policies can be a major impediment to placing capital.

- **Competition with donor funding**: Grant financing is widely available from donors active in Tanzania. At times, impact investors compete with grant capital as entrepreneurs who seek capital are typically also aware of donors. Donor presence in the market can complicate negotiations for commercial capital as entrepreneurs may believe they can raise free capital or may believe investor return expectations are too high.
• **International decision makers:** Many impact investors have investment committees based abroad that include international decision-makers who may not have experience with investments in East Africa. These remote investment committees interpret risk differently than do their investment teams operating on the ground, creating friction between investment officers forming relationships with entrepreneurs and investment committees making the ultimate investment decisions.\(^\text{30}\)

• **Long diligence process:** Correlated with the lack of investment-ready deal flow and international decision making, the diligence process for impact investors can often stretch 12-18 months for both debt and equity investments.\(^\text{31}\) This lengthy process can damage relationships with entrepreneurs, who often view it as reflecting a lack of trust. It can put additional pressure on businesses and lower long-term returns as companies must survive without needed capital, creating a significant opportunity cost as management teams spend time courting investors.

• **Few exit examples:** For new funds looking to raise capital, the youth of the industry means there are few successful exit examples. Without a successful track record, it can be difficult for impact fund managers to raise a second fund—some interviewed for this report believe it may be easier for a new fund manager to raise funds than for an experienced one to do so.

• **Limited experienced local talent:** Impact investors struggle to find experienced local staff to support both their own investment teams and management teams within growing portfolio companies. This challenge is particularly acute for finance professionals with 5-15 years of experience who can serve as a company CFO, investment officer, or portfolio manager for an impact investor, despite the large number of students graduating each year with degrees in accounting and finance. Even when a talented, experienced professional can be found, they often command high wages that can be challenging for SMEs or social enterprises to support, especially in their early years. Similarly, lean impact investors, particularly those operating small funds, find it difficult to pay high wages. This shortage is particularly acute in Tanzania, as the diaspora has not yet begun to return to the country.

• **Difficulty accessing local currency instruments:** Many social businesses engage with disadvantaged populations, often earning the majority of their revenues in local currencies. However, most impact investors track returns in international hard currencies and have little ability to invest in local currencies. This is especially challenging for long-term debt instruments, which require repayment in hard currencies that can appreciate 5-10% per year. Hedging options are expensive at both the individual investment level and at the fund level, although some impact investors report effectively using fund level hedges to minimize risk. Please see the East Africa regional chapter for additional detail on the dynamics of local currency investments.

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\(^{30}\) Based on primary and/or secondary research conducted during this study; see “Introduction and Methodology” chapter of this report for details.

\(^{31}\) Based on primary and/or secondary research conducted during this study; see “Introduction and Methodology” chapter of this report for details.
Opportunities

Despite these challenges, there are many opportunities for non-DFI impact investors to operate in Tanzania effectively and leverage return-seeking investments to drive job creation, economic development, and opportunities for disadvantaged populations. Opportunities for impact investors in Tanzania include the following:

• **Leverage TA facilities for pre-investment pipeline building:** Many impact investors have successfully raised technical assistance facilities for portfolio companies. Increasingly, TA funders such as USAID and DFID recognize the importance of pre-investment support to get companies to the point where they can pass rigorous investment committee requirements. Targeted, tailored support requires an upfront commitment of resources but impact investors report that it has proven effective in preparing targets for investment and building high quality deal flow. This support can dramatically reduce diligence timelines if the investor is able to increase familiarity and visibility into the business pre-investment in order to assess the company’s operations and ability to execute.

• **Ease rigid investment criteria:** Impact investors in Tanzania repeatedly stressed the need for more flexible non-financial investment criteria. Rigid criteria around sector, impact, and stage of business are generally seen as impediments to investing in the few investment-ready opportunities that arise. Without the volume of high-potential entrepreneurs and opportunities in Tanzania as in, for example, Kenya, impact investors benefit from being able to place capital where opportunities arise, rather than focusing on a sub-set of opportunities.

• **Increase local decision-making:** Where possible, impact investors cited significant improvements in their portfolios through local decision-making and in-country support. This allows investment officers to form meaningful relationships with portfolio companies, where they are empowered to quickly respond to realities on the ground.

• **Source opportunities outside major cities, like Dar-es-Salaam:** Though impact investors with staff on the ground in major cities already report an easier time finding investments than those based abroad, many entrepreneurs operating in rural areas do not spend much time in Dar-es-Salaam. For impact investors who see these types of businesses as highly impactful, it will be increasingly necessary to build relationships beyond those made in economic centers.

• **Innovate with new models of investment vehicles:** The Tanzanian impact investing community is innovating and experimenting with interesting new models. For example, DFID recently established an impact capital vehicle focused specifically on agricultural companies in the Southern Agricultural Corridor of Tanzania (SAGCOT) that is currently raising capital. This narrow geographic and sector focus will create detailed market awareness and push concentrated capital into this challenging region with a high potential for impact.
In addition, impact investors in Tanzania see specific opportunities in the following sectors:

- **Agriculture**: Overwhelmingly, impact investors identify agriculture as a key opportunity. Tanzania is the third largest country by area in the region and there is ample arable land. Impact investors note that working directly with smallholders can be difficult given their willingness to change crops or side-sell, and they see significant opportunity in agricultural processing and post-harvest marketing and infrastructure, including warehousing, cold storage, and transport.

- **Renewable energy**: Large segments of the Tanzanian population lack reliable access to grid power, opening opportunities for micro-grid and off-grid solutions. However, entrepreneurs must be wary of potential government regulation. For example, the government at one point considered lifting VAT exemptions on solar products, but it has since confirmed the exemption.32

ABOUT THE GLOBAL IMPACT INVESTING NETWORK

The Global Impact Investing Network (GIIN®) is a nonprofit organization dedicated to increasing the scale and effectiveness of impact investing. The GIIN builds critical infrastructure and supports activities, education, and research that help accelerate the development of a coherent impact investing industry. For more information, see www.thegiin.org.

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