

Analysis of macroeconomic determinants of tax revenue in Tanzania (1990-2022)

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Abstract

The study aimed to analyze the macroeconomic determinants of tax revenue in Tanzania using secondary data over 33 years. We used a quantitative approach analyzing data collected from Bank of Tanzania (2024) and World Bank (2024) through descriptive statistics, graphical and inferential statistics analysis. In the inferential statistics analysis, tax revenue was treated as the dependent variable and inflation, import expenditure, export volume, and foreign direct inflows as independent variables. Inflation, export volume, and foreign direct investment inflows negatively impacted tax revenue, while import expenditure had a positive effect. In the short run, there was no significant relationship between these variables, but significant relationship was found in the long run. To stabilize or increase tax revenue, the study recommends controlling inflation through monetary policy, evaluating foreign direct investment and export tax incentives, optimizing import tariffs, and streamlining customs processes to improve tax collection without hindering trade.

Keywords: Tax revenue, inflation, imports, export volume, foreign direct investment

JEL Code: H2, E31, F21

1.0 Introduction

Worldwide tax revenue mobilization has been a great concern because the revenue derived from taxes finances daily activities (Prowd & Kollie, 2021). Governments have a responsibility to raise funds in order to support social programs, health care, education, and capital projects and among major sources of government funding in both developed and developing nations is tax revenue (Yaru & Raji, 2022). The necessary funds are produced through taxes so that the country can fulfill its fundamental duties to its citizens. Any nation's ability to grow and develop depends primarily on how much tax revenue can be raised to fund infrastructure (Prowd & Kollie, 2021).

Developing countries must rely heavily on domestic revenue mobilization because over-reliance on foreign financing may eventually result in issues with debt sustainability. Over the past 25 years, developing nations' experiences with domestic resource mobilization have been a challenge (Sen Gupta, 2007). Tanzania has initiated different measures and policies to improve voluntary tax compliance like automation tax payment process, outreach of tax services and education, enactment of tax laws and regulation for enforcement and reorganizing revenue authority (Mzalendo & Chimilila, 2020). The

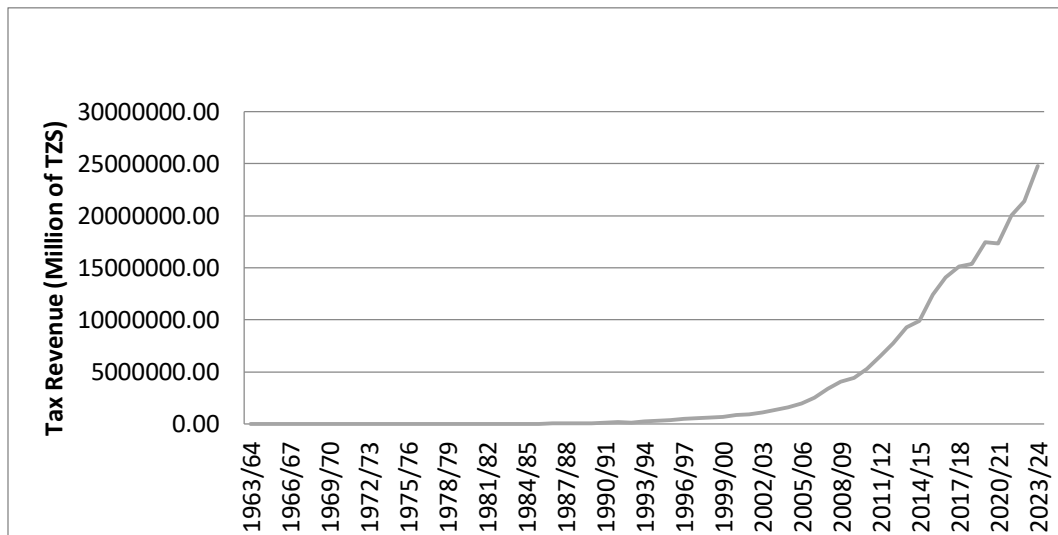
government currently established a tax on digital money transaction to support recurrent and capital expenditure (Mshomba, 2021). Tanzania’s revenue collection experienced an average growth rate of 25.9 percent within ten (10) years (Bank of Tanzania, 2024).

Table 1: Change in government revenue for selected years

Year	Amount	Percentage change
2010/11	1,546.22	17.7
2011/12	1,095.06	10.7
2012/13	2,592.76	22.8
2013/14	1,901.29	13.6
2014/15	-408.84	-2.6
2015/16	4,943.68	32
2016/17	-677.31	-3.3
2017/18	2,224.23	17.2
2018/19	2,107.47	9.6
2019/20	-880.24	-3.7
2020/21	6,010.09	25.9

Source: Bank of Tanzania (2024)

Between the fiscal years 2009/2010 and 2020/2021, Tanzania's government revenue collection experienced a growth of 25.9 percent. Table 1 indicates that overall government resource collection rose from 2009/10 to 2020/21, except in the years 2014/15, 2016/17, and 2019/20. The most significant change was observed in 2015/16, with a recorded increase of 32.0 percent. Resource envelopes experienced an increase from 2009/10 to 2020/21, notwithstanding a minor decrease in revenue collections during 2014/15, 2016/17, and 2019/20. During the past three years, the period of 2020/21 experienced a notable increase of 25.9 percent (Bank of Tanzania, 2021). The government of Tanzania is facing challenges in optimizing its tax revenue despite favorable economic conditions. Specifically, there is a significant gap between projected and actual tax revenue collection.



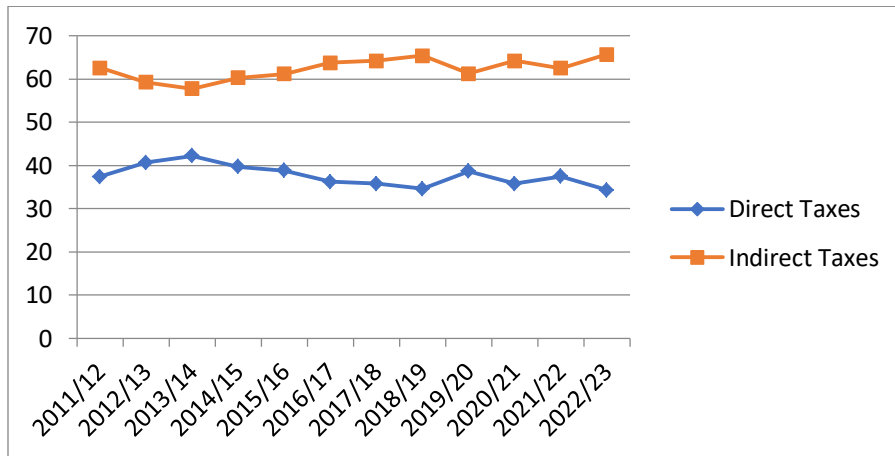
Source: Bank of Tanzania (2024)

Figure 1: The trend of tax revenue in Millions of TZS

This discrepancy has been caused by different factors like non-compliant taxpayers, tax evasion and avoidance as well as administration challenges although the government has tried as much as possible to eliminate the problem through the establishment of Tanzania revenue authority, expanding the tax bases, creation of new sources of revenue, promoting voluntary tax compliance but with all this measures the problem still exist. Figure 1 provides a good insight of the trending of tax revenue collection in Tanzania for a period of over six decades.

There is an upward trending of tax revenue from earlier 2000s. The tax used is nominal tax which uses the current prices. As a result, the increasing inflation is reflected in the amount of tax revenue collected. But, there are other factors explaining increasing trend of tax revenue like population growth. In this we know that population during periods of colonial independence was far lower than the population in the 2000s. The amount of tax revenue in 1960s is not even visible in Figure 1 due to low nominal values and even the VAT was not yet introduced. The VAT which was introduced after the introduction of TRA had brought a significant transformation in tax revenue collection. This part of indirect tax has a significant share.

The government relied mostly on direct tax thereby collecting a limited amount of revenue from employees and other products and properties in a very difficult way. Collecting tax required a large number of tax collectors who went from one household to another. People during that time used to run away from home escaping tax payment. The introduction of TRA brought in the simplification in collecting tax by focusing on indirect tax.



Source: URT (2024)

Figure 2: The trend in the share of direct and indirect taxes

From Figure 2, the share of indirect tax has been consistently higher than the share of direct tax. This is due to increased manufacturing activities and other services. In general there are increased economic activities leading into increased production of goods and services. The retail businesses and other services contribute to the growing of indirect tax as compared to the direct tax. Even for the direct tax (URT, 2024) a large portion come from pay as you earn. This amount keeps expanding with increasing level of employment. Now, if we compare the period of independence and the period we are in now, the number of employees have tremendously increased and the wage rate has significantly improved. As a result, the tax revenue prior to the initiation of Tanzania Revenue Authority must be very low compared to the period after the it was introduced. amount used to meet current and development expenditure of the time together with non-tax revenue. Even with the increasing tax revenue collection, the government is still not self-sufficient in financing current and development expenditure.

2.0 Literature Review

The Laffer curve theory developed by Arthur Laffer, posits that there's an optimal tax rate maximizing government revenue. Higher tax rates beyond a certain threshold discourage work and economic activity, leading to reduced tax income (Laffer, 1974). Effective tax administrations maximize revenue. Advanced technology, and skilled staff can ensure more tax collection, but political and economic constraints (Bikila, 2021). Taxes should be based on an individual's ability to pay, ensuring fairness and equality. Progressive taxation is criticized for potentially being unjust and reducing incentives to earn more. But taxes should base on benefits received from government operations. However, free-rider problem where individuals underreport benefits reduce tax liability (Chigbu, et al., 2012).

AL-Qudah (2021) analyzed tax income in Jordan from 1990 to 2019 using ARDL models. They uncovered long-term correlations between government expenditure, per capita GDP, and tax revenue. But foreign assistance negatively impacted tax revenue. Ayenew (2016) investigated tax revenue in Ethiopia from 1974 to 2013. Using Johansen co-integration, the study found real GDP per capita income, foreign assistance, and industrial value-added positively impacting tax revenue in the long-term, while inflation has adverse effects. Minh Ha *et al.* (2022) studied tax revenue determinants in Southeast Asia. They found that official development assistance negatively impacted tax revenue, recommending refining of trade policies, attracting FDI, and effective management of foreign assistance and debt.

Hlongwane et al. (2022) examined factors affecting South Africa's tax revenue from 1972 to 2021 using ARDL models. They found that tax revenue was positively affected by government spending, while negatively influenced by trade and inflation. They recommended revising trade and inflation policies and enhancing government spending. Terefe & Teera (2018) analyzed East African nations' tax revenue. They revealed a positive influence of GDP, foreign assistance, and trade openness on tax revenue. From their findings, they suggested maintaining a stable macroeconomic environment and low inflation for sustained revenue growth.

Ibrahim and Jairo (2023) studied tax revenue performance in EAC countries (2009-2018) using panel data. Found administrative efficiency positively affects revenue performance. Recommended improving tax administration through increased personnel and enhanced institutional quality. Rwechungura (2016) analyzed factors influencing Tanzania's tax revenue (1997-2015) using regression models. The findings show that urbanization and services positively influence tax revenue, while exchange rates have negative effects, suggesting improving tax collection systems and addressing factors like inflation and trade openness.

Several studies (AL-Qudah, 2021; Ayenew, 2016; Minh Ha et al., 2022; Hlongwane et al., 2022; Terefe & Teera, 2018) have worked on the determinants of tax revenue, some focused on sub-Saharan Africa and others in Asia. But in Tanzania the similar study on tax revenue and its macroeconomic determinants was done by Rwechungura (2016). The findings of this study revealed that, two variables which are urbanization and service were positively and statistically significant in influencing domestic revenue, revenue collected from large taxpayers, and total tax revenue. The study was limited to an 18 years period focusing on short-run rather than long-run relationship by employing a multiple regression model. The current study bridges this gap by using vector error correction model for a period of 33 years.

3.0 Methodology

3.1 Data and Data Source

The study used a quantitative research approach and employed an explanatory research design, primarily relying on secondary data sources. Data in regard to tax revenues were collected from TRA's website and data in regard to elements of tax base and structured factors were collected from World Bank's website. Table 2 displays the maximum and lowest values for each variable listed. The table presents the mean and standard deviation for all variables. A greater standard deviation indicates more diversity among the individual data points. The values are given in logarithm form except for the tax revenue.

Table 2: Descriptive Summary Statistics

Variable	Observation	Mean	Std. Dev	Min	Max
TR	33	5991040	6792847	118257	2.14e+07
INFL	33	11.58606	9.458317	3.29	35.83
IMP	33	6.270606	4.547483	1.6	14.8
EXPV	33	4.707576	3.595535	0.51	11.64
FDIINFL	33	0.7533333	0.5975819	0	2.09

Source: Bank of Tanzania (2024); World Bank (2024)

Tax Revenue (TR) variables exhibited a mean value of approximately 5,991,040 LCU, with a minimum increase of 118,257 in local currency unit (LCU) in 1990 and a maximum value of 21,400,000 LCU in 2022. The standard deviation was 6,792,847 LCU, which exceeds the mean, indicating significant deviation from the mean. INFL (Inflation rate) variable was found to have the mean value of approximately 11.59 percent from 1990 to 2022, inflation was at minimum 3.29 percent in 2020 while the maximum of 35.83 percent in 1990 with the standard deviation of 9.46 percent which is less than the mean implying the less deviation from the mean. IMP (Imports) variable was found to have a mean value of approximately 6.270606 USD for the period of 33 years, while import was increasing at minimum value of 1.6 in 1990 and maximum value of 14.8 in 2022 with the standard deviation of 4.547483 USD which is less than the mean value implying the less deviation from its mean. EXPV (exports volume) had a mean value of 4.707576 for the period of 33 years while the exports volume growing at minimum value of 0.51 in the year of 1991 and maximum growth of 11.64 in the year of 2022 with the standard deviation of 3.595535 which is less than the mean value indicates the less deviation from its mean. FDIINFL (Foreign Direct Investment Inflows) had a mean value of approximately 0.753333 from 1990 to 2022 while foreign direct investment inflow was at 0 USD minimum value in the years of 1990 and 1991 and 2.09 maximum value in the year of 2013 with the standard deviation of 0.5975819 which is lower than the mean value implying the less deviation from its mean.

3.2 Model

The econometric technique used to analyze the relationships between dependent and independent variables was vector error correction model (VECM). The study used VECM to determine the relationship between dependent and independent variables in log-run and short-run. Therefore, the regression was run with single dependent variables and four independent variables which were Inflation (INFL), Imports (IMP), Export Volume (EXPV) and Foreign Direct Investments (FDIINFL) with econometric model as equation (1) below.

$$TR = f(INFL, IMP, EXPV, FDIIFD) \quad (1)$$

Assuming the relationship in equation (1) takes on the Cobb-Douglas formulation, the linear model is obtained through introduction of natural logarithm to be linear in parameter as in equation (2) below. This functional equation (2) is economically formulated as accruing to Ayenew (2016).

$$\ln(TR)_t = \beta_0 + \beta_1 \ln(INFL)_t + \beta_2 \ln(IMP)_t + \beta_3 \ln(EXPV)_t + \beta_4 \ln(FDIIFD)_t + \mu_t \quad (2)$$

Where, TR stands for tax revenue, INFL is representing inflation, IMP represents Imports, EXPV is the export volume, and FDIINFL is for foreign direct investment inflows. Equation (2) is linear in parameter and shows the long run relationship which are obtained through ordinary least square approach. But since most time series data suffer from unit root problem, the study started by testing the data for unit root problem. The unit root testing model for every variable as shown in Waryoba (2023) can be generally written as in equation (3) below.

$$\Delta X_t = \beta_1 + \beta_2 t + \delta X_{t-1} + \sum_{i=1}^m \alpha_i \Delta X_{t-i} + \varepsilon_t \quad (3)$$

Equation (3) is the Augmented Dickey-Fuller Model (ADF) which assumes that the error term is correlated with its previous values. That is why dependent component is taken in the right hand side with its lagged values to offset the serial correlation. The number of lags (m) is selected to get the right model for the test. There are three possibilities in the displayed model (see Waryoba, 2023). One possibility is when the variable is trend stationary where a trend variable (t) is included to become stationary. Another possibility is when the variable is random walk where both constant parameter and trend variable are omitted from equation (3). Lastly but not least is when the variable is a random walk with drift where a trend variable is removed in equation (3).

From the test, all the variables were non-stationary and of the same order calling for a Co-integration analysis. Running non-stationary variables using OLS may result into spurious regression. To avoid this problem, the study implemented Johansen and Juselius co-integration test (Johansen, 1988; Johansen & Juselius, 1990) which is according to equation (4).

$$\Delta Y_t = \beta_1 + \beta_2 + \Pi Y_{t-1} + \sum_{i=1}^{k-1} \Gamma_i \Delta Y_{t-i} + \phi D_t + \varepsilon_t \tag{4}$$

Where, $\Pi = \sum_{i=1}^q A_i - I$ and $\Gamma_i = -\sum_{j=i+1}^q A_j$ are more explained in Waryoba (2023) and Olorogun (2021).

Once we get a co-integrating equation, Engle & Granger (1987) suggested establishing an error correction model (ECM). As expressed in equation (5), the vector ECM allows for long-run stability and short-run dynamics.

$$\begin{aligned} \Delta \ln TR(t) = & \beta_1 \Delta \ln TR(t-1) + \beta_2 \Delta \ln INFL(t-1) + \beta_3 \Delta \ln IMP(t-1) \\ & + \beta_4 \Delta \ln EXPV(t-1) + \beta_5 \Delta \ln FDIINFL(t-1) + \lambda_i ECT(t-1) + \varepsilon_t \end{aligned} \tag{5}$$

Equation (5) is the empirical mode estimated in this study. The *ECT* stands for error correction term. Its coefficient determines the speed of adjustment to reach into equilibrium.

4.0 Results and Discussion

4.1 Results

The unit root test was carried out to find the order of integration to allow VECM. This is because if variables are in the same order of integration, they can be co-integrated and co-integrated variables will mostly fit the VECM. Due to the presence of non-stationarity in several variables at levels, the ADF unit root test was employed to pre-test these variables, assessing their order of integration and stationarity initially at the level and subsequently at the first difference. Unit root tests are utilized to evaluate the alternative hypothesis, which claims the absence of a unit root and the stationarity of variables, against the null hypothesis, which maintains that all variables in a time series contain a unit root and are consequently non-stationary.

Table 3: ADF Unit Root Test Results at Level

Variables	Level	First difference	Integration order
	Test Statistics	Test Statistics	
TR	3.494	-3.326	<i>I</i> (1)
INFL	-2.557	-4.857	<i>I</i> (1)
IMP	-0.722	-3.249	<i>I</i> (1)
EXPV	-0.072	-4.707	<i>I</i> (1)
FDIINFL	-1.928	-9.007	<i>I</i> (1)
Critical Value (5%)	-2.986	-2.989	

Source: Bank of Tanzania (2024); World Bank (2024)

All variables were non-stationary based on the Augmented Dickey-Fuller Unit Root Test, as shown in column 2 of Table 3 suggesting a unit root issue with the variables. The findings show that the p-values are higher than the 0.05 significance threshold and the absolute values of the test statistics are lower than the critical value for every variable. As a result, we did not rule out the null hypothesis that a unit root exists. After differencing, all the variables became stationary as in the third column of Table 3 where all the test statistics are absolutely larger than the critical value at 5 percent. Since the null hypothesis of a unit root was rejected at the 5 percent significance level, all variables were deemed stationary after the first difference. This shows that the variables are integrated of order one, that is $I(1)$ as in the last column of Table 3.

The results in Table 4 show that the error correcting term has the required sign, which is negative and significant at the 5 percent levels of significance. It is suggested that stability is being adversely altered by the error correcting term coefficient. 10.28 percent is the yearly rate of adjustment required to bring about long-term balance. It will take around ten years to recover completely from a single shock and achieve long-term stability because of the slower pace of adjustment.

Table 4: Short run results

Variables	Coef.	Std. Error	Z	P-Value	[95% Conf. Interval]	
_cel	-0.1028178	0.0377544	-2.72	0.006	-0.1768149	-0.0288206
TR	-0.0536941	0.2142232	-0.25	0.802	-0.4735638	0.3661756
INFL	0.0274091	0.0478666	0.57	0.567	-0.0664077	0.121226
IMPE	0.0036686	0.1181949	0.03	0.975	-0.2279891	0.2353264
EXPV	0.1835594	0.1903069	0.96	0.335	-0.1894353	0.556554
FDIINFL	-0.0285495	0.0324751	-0.88	0.379	-0.0921995	0.351005
_Constant	0.0987161	0.0288298	3.42	0.001	0.0422107	0.1552215

Source: Bank of Tanzania (2024); World Bank (2024)

However, all independent variables' short-term outcomes showed that they had no discernible effect on tax revenue. Inflation, imports, and exports were all positive but negligible at the 5 percent threshold of significance. But foreign direct investment was negligible and negative and this because economic activities stemming from inflation, trade and investments may take time to influence tax revenue. The study employed the Johansen Normalization from VECM to measure the influence of some of macroeconomic variables on tax revenue. The table below demonstrates the normalization cointegration in the long run relationship between variables.

Table 5: Long run relationship with TR as the dependent variable

Variables	Coef.	Std. Error	Z	P> Z	[95% Conf. Interval]	
INFL	-.8902517	0.1421564	-6.26	0.000	0.6116303	1.168873
IMP	2.532514	0.391954	-6.46	0.000	-3.30073	-1.764299
EXPV	-1.068477	0.4600632	-2.32	0.020	0.1667692	1.970184
FDIINFL	-.25344	0.886967	-2.86	0.004	0.0795977	0.4272824
Constant	14.43726

Source: Bank of Tanzania (2024); World Bank (2024)

From the Table 5 above those were the empirical outcomes of the cointegration coefficient from which a conclusion is drawn about Tanzania's long-run association between Tax revenue and some of macroeconomic variables like inflation, imports, export volume and foreign direct investments inflows. Under ceteris paribus, inflation, imports, export volume, and foreign direct investment are statistically

significant at the 5 percent level, suggesting that these variables have impacted tax revenue in Tanzania from 1990 to 2022. All variables were statistically significant, demonstrating their potential to influence tax revenue in Tanzania during the specified study period. When inflation, imports, export volume, and foreign direct investment inflows are all zero, tax revenue increases by an average of 14.44 percent, assuming other variables remain constant. This indicates that the aforementioned macroeconomic factors are significant in determining tax revenue during a specified period.

4.2 Discussion

The inflation coefficient was determined to be negative and statistically significant at 5 percent levels of significance. This suggests that 100 percent increase in inflation will lead to 89.03 percent decrease in tax revenue, assuming all other variables are held constant. The rise in inflation adversely affects the economy and, subsequently, tax revenue. Although nominal revenue may increase during inflation, the real value of that revenue, when adjusted for inflation declines. This diminishes the government's purchasing power, resulting in a reduced capacity to fund goods and services with the same financial resources. This contradicts Calvo & de la Cruz (2024) who found increasing inflation leading into increasing nominal tax revenue across Europe. High inflation can influence taxpayer behavior, prompting investors to reallocate their investments towards less taxed assets or individuals to modify their spending patterns to mitigate higher taxes, such as decreasing consumption of taxable goods. This may lead to a decrease in total tax revenue for a specific duration.

In the long run, imports had a positive and significant effect on tax revenue. Assuming all other variables remained constant, a 1 percent increase in imports leads to 2.53 percent increase in tax revenue. This indicates that increased imports results in higher tax revenue. Imports affect tax revenue in several ways, including customs duties. As the volume of imports rises, the government collects increased tariff revenue. Higher tariffs on specific goods directly enhance tax revenue. Additionally, value-added tax on imports, excise taxes, and customs processing fees contribute to an overall increase in tax revenue through importation. Increased imports by a country lead to greater opportunities for revenue generation through various taxes and fees. This reflects what Waryoba (2018a) found on the effect of import base on tax revenue. An increase in import base increases tax revenue and reduces discretionary measures which deter tax revenue increments.

The results indicate that at 5 percent significance level, export volume is negatively and statistically significant in influencing tax revenue. A 1 percent increase in exports is associated with a 1.068 percent decrease in tax revenue in the long run, holding all other variables constant. The negative coefficient indicates that an increase in exports correlates with a decline in tax revenue due to various factors, including government policies that offer tax incentives, subsidies, and exemptions to promote exports. In order to increase export performance (Waryoba, 2018b) China undertook exchange rate revaluation. So, even policies on tax incentives are implemented to encourage more exports as a way to reduce trade deficit. These policies decrease the tax burden on exporting businesses, resulting in reduced tax revenue. A country may seek to enhance exports by implementing lower taxes on export-related industries or offering exemptions from VAT, sales tax, and other levies to improve international competitiveness. However, this approach can lead to a reduced tax base and, consequently, lower tax revenue. A negative coefficient of exports indicates a trade-off between increasing exports and decreasing tax revenue, likely resulting from tax policies that prioritize exports, thereby diminishing direct tax collection from export activities.

At 5 percent level, long-run coefficient of foreign direct investment inflows was negative and statistically significant, showing that a 1 percent increase in flows decreases tax income by 0.253 percent. Increasing foreign direct investment lowers tax income over time. This is contrary to what is expected because Waryoba (2017) found that foreign direct investment supported productivity in China even during the Asian financial crisis. If economic growth influenced tax revenue, then foreign direct investment is supposed to support tax revenue growth. However, the contrary results could be due to foreign corporations

repatriating earnings leading into the host country's taxable base decline. This results in decreased tax revenue from profits generated by foreign direct investment firms, despite their contributions to economic growth. Additionally, practices such as transfer pricing and tax avoidance are prevalent among multinational corporations engaged in foreign direct investment. These firms often shift profits to low-tax jurisdictions, thereby diminishing their taxable income in the host country and resulting in lower tax revenue. Furthermore, tax incentives offered to foreign investors, including significant tax breaks, reduced corporate tax rates, exemptions from VAT and other taxes, or even tax holidays, contribute to minimal tax revenue from these companies, ultimately leading to a net reduction in overall tax revenue.

5.0 Conclusion

The main objective of this study was to analyze the macroeconomic determinants of tax revenue in Tanzania for the period of 33 years (1990-2022). In Tanzania, tax revenues can be categorized according to the department they are collected from. This study used four factors on determining tax revenue in Tanzania. The study employed the total of five variables as independent variables and one variable as dependent. Independent variables used are Inflation, imports, Exports and foreign direct investment inflow. Empirical results of regression revealed that inflation, exports volume and foreign direct investment inflows were negatively statistically significant while import expenditure was positively statistically significant influencing tax revenue.

From the findings, in order to achieve the relationship between tax revenue as dependent variable and independent variables like inflation, imports, export volume and foreign direct investment inflows the study recommends as follow. Since inflation has negative impact on tax revenue, government and policy makers should focus on controlling inflation to stabilize or increase tax revenue through monetary policy where the central bank can use interest rates and other monetary tools to keep inflation in checks. Also, the use of tax indexation through adjusting tax brackets or tax structure for inflation can prevent a decline in real tax revenue. Furthermore, the government and policymakers should take a price control in extreme cases temporary price control might help to stabilize inflation but these needs to be balanced against the potential negative side effect like shortages.

Since there is positive relationship between imports and tax revenue the government could optimize tax revenue through optimizing import tariffs by reviewing and adjusting imports tariffs to balance revenue generation without discouraging essential imports. Also, customs process should be streamlined to improve customs and tax collection system at ports and One Stop Boader Post (OSBP) to ensure efficient tax revenue collection without hindering trade. Furthermore, promoting consumer demand through encouraging domestic consumption of imported goods, as this can directly boost tax revenue through import duties.

With a negative influence of export volume on tax revenue, it's possible that overly generous tax breaks are eroding tax base. The export tax incentives should be evaluated to review the effectiveness of exports tax incentives and ensure they are targeted towards industries that offer long-term economic benefits. Also, there should be a based- performance incentive instead of broad tax breaks, there should be conditional incentives where companies only get benefits if they meet certain performance criteria like job creation and local reinvestments.

The negative influence of foreign direct investment on tax revenue suggests that the tax incentives given to attract foreign direct investment might be too generous. Now the foreign direct investment incentives should be reformed through reducing or refining tax breaks for foreign investors, ensuring that they are time-bound or conditional on substantial economic contribution like job creation and local procurement. Also, the multinational companies should be monitored so as to prevent tax avoidance or profit-shifting practices especially in sector of high foreign investment.

Promotion of domestic investments so as to reduce reliance of foreign direct investment, the policymakers and government should encourage domestic investment and entrepreneurship by providing tax incentives to small and medium-sized enterprise to stimulate domestics, job creation and entrepreneurship which can generates stable long-term tax revenue. Furthermore, reviewing and limiting foreign direct investment tax holidays, the long-term tax exemption offered should be reviewed and implemented time-limited or conditional incentives based on technology transfer and reinvestment into local economy.

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