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Factors Determining the Development of the Tanzanian Private Equity Market

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Preface

This master thesis represents the completion of our MBA program at the University of Agder. Our interest in Tanzania, and motivation for choosing this specific topic started as we both had the opportunity to stay in Tanzania for one semester the fall of 2018. The University of Agder Internship Abroad Programme offered us a unique opportunity to gain experience from working and studying in a high growth economy.

We would like to thank Professor Trond Randøy who has been our supervisor, and guided us through this project with valuable input and support throughout the entire master period. We also appreciate the guidance and directions of Dr. Neema Mori, a senior lecturer at the University of Dar es Salaam Business School.

Abstract

The global private equity industry has experienced continuous growth in the last decade, and we have witnessed an even stronger growth in East Africa. However, Tanzania has not been following these trends, and despite the exceptional economic growth of the country, it lags behind in attracting private equity deals. This research aims to provide an understanding of the underlying reasons for the low private equity activity by studying potential factors affecting the development of the private equity market in Tanzania. The primary research question seeks to explain the factors and the way they affect private equity allocation decisions. The secondary objective of this study is to highlight the policy implications specific to Tanzania that could make the country more attractive for private equity investments. This research aims to complement the underdeveloped academic literature on private equity activity in Tanzania, where we build on the framework presented by Groh, Liecthenstein, Lieser, & Biesinger, (2018) to rank a country's attractiveness for private equity investors. A qualitative approach was utilized to find the relative importance of the factors, assigned by actual private equity investors. The main findings from this study, guided by the theoretical framework, are that tax rates, availability of debt, exit opportunities, quality of legal enforcement, education and human capital, and deal opportunities are the most important factors that contribute to explaining the development of the Tanzanian private equity market. In addition, two new factors, political stability and investor's perception of a country, emerged during the research and were also considered as important allocation criteria for private equity investors. The results of this study indicate that there are five key areas in need of improvement; legal system, tax system, administrative burdens, education system, and infrastructure. It was suggested that an increased effort from the policymakers to focus on, and improve these areas could increase the country's attractiveness for private equity investors.

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1. Introduction

1.1 General Introduction

In Africa, private equity (PE) investments play a critical role in facilitating resources to evolve individual companies and ecosystems, especially in relation to the shallowness of African capital markets and the high cost of debt financing (The economist , 2017). The rapid economic growth in many of the African countries and other emerging markets attract investors as they seek opportunities for higher returns. However, many investors struggle to determine where, how and with whom to invest. Although there has been a strong growth in PE activity in recent years, the share of PE capital allocated to emerging markets remains low relative to developed markets (IFC , 2012). Groh, (2009) implies that expected economic growth is not all that matter for investors, and that the PE industry is of a complex nature with a large variety of criteria that affect PE funding. Therefore, it is interesting to study potential factors affecting allocation decisions for PE investors in emerging markets, and in our case, with a particular focus on the Tanzanian PE market.

Olomi & Mori, (2015) argue that access to affordable long-term finance is one of the biggest barriers to the development of small and medium enterprises (SMEs) in Tanzania. In addition, debt financing has a relatively short maturity, which may cause problems for startup firms. Contrarily, equity financing can with a longer maturity offer an opportunity for enterprises to raise capital, share risks, and complement knowledge and skills. PE investments have in the recent past experienced strong growth, and have accelerated sharply in both developed and emerging economies. The role of PE is increasingly becoming important as high growth potential companies utilize the alternative source of finance, in addition to receiving strategic advice (Gatauwa, 2014). According to Gompers & Lerner, (2001) PE has developed as a vital intermediary in financial markets by providing capital to firms that might otherwise have difficulties attracting financing. The characteristics of these firms are their small size, young age, high levels of uncertainty, and informational asymmetries. Therefore, especially for countries like Tanzania, where SMEs account for a significant share of production and employment (Matambalya & Wolf , 2001), PE activity contributes to economic development.

1.2 Research Problem

In the years 2015 and 2016, USD 1.1 billion were raised for PE investments in the East African region, indicating a 41 percent growth from the previous period 2007-2014. In the same years, it was reported a total of 36 PE backed deals with an estimated value of over USD 600 million, implying that there is still a lot of capital yet to be deployed by PE funds in East Africa. This steep growth can be attributed to the increasing participation of regional pension funds in PE investment, and the region's economic growth which has led to an increase in the number of strong private enterprises that have scalability (KPMG & EAVCA , 2017). Despite this growth in the East African region, the supply of PE in Tanzania seems to lag behind. AVCA, (2018) ranks Tanzania to be the 8th most attractive country for PE investment in Africa over the next three years, while its neighbouring country, Kenya, is in second place. The PE industry seems to be underdeveloped in Tanzania, as it has not sufficiently adapted to the local institutional environment (Olomi & Mori , 2015). Tanzania is a country with great potential and high GDP growth (World Bank , 2017), therefore, it is interesting to study the reasons for the low PE activity and the factors affecting institutional investors decisions when allocating capital into Tanzania.

1.3 Research Objective

The determinants of dynamic PE markets have been extensively studied in academic literature. Gompers & Lerner, (1997) and Jeng & Wells, (2000) are among the first and most known to study the determinants of PE activity. The findings reveal a complex nature of the factors influencing PE decisions, and the researchers struggles to reach a consensus on the most important factors for attracting PE capital across countries. However, Groh et al., (2018) have lately provided substantial effort to compile several leading factors suggested from previous literature that shape national PE markets, and proposes one single composite measure. Their work led to the creation of the Venture Capital (VC) and PE Country Attractiveness Index. The factors below illustrate the structure of their index as each present one of six key drivers of a country's attractiveness for investors:

1. Economic Activity
2. Depth of Capital Market
3. Taxation
4. Investor Protection and Corporate Governance
5. Human and Social Environment
6. Entrepreneurial Culture and Deal Opportunities

The factors also include different subsets that capture and measure the different elements driving the main component. Each of the six factors have varying numbers of subsets and are assigned weights of importance based on the number of subsets each factor inhabits in the attractiveness index. There are 22 subsets in total and each is assigned an equal weighting, hence economic activity that has 3 subsets receives a weight of 3/22. Unfortunately, these six factors are not directly measurable, thus best proxies are used as estimates for a quantitative approach to measure and rank the countries attractiveness. Groh et al., (2018) acknowledge that the composite measure can deviate from the actual PE activity since investors are often influenced by herd mentality and trends to certain markets, especially driven by growth expectations.

This research aims to complement the still thin layer of academic literature on PE activity in Tanzania, where we build on the previous work of Groh et al., (2018). The objective of this study differs from Groh et al., (2018) as we aspire to find the relative importance of the drivers assigned by actual PE investors, and how they affect PE investment decisions, through empirical research using a qualitative approach. The scope of the study is limited to only include Tanzania. This thesis seeks to answer the following research questions:

1. *What are the drivers that underpin the development of the PE market in Tanzania?*
2. *What are the policy recommendations to improve Tanzania's ability to attract PE investments?*

The goal is to increase the knowledge of the key drivers for PE investment and propose suggestions on how to facilitate a better investment climate for Tanzania as a developing country.

The rest of the thesis is structured in the following manner. In the next chapter, we go through the basics of PE, and the PE situation both globally, and with a narrower focus on the African region and Tanzania. In chapter three, we present some of the theoretical background and review previous literature on the subject. The methodology will be presented in chapter four, followed by a presentation of our findings in chapter five. We will analyse and discuss our findings in chapter six before we summarize our work in chapter seven.

2. Background and Relevance of the Study

2.0 Introduction

In this chapter, we will discuss the relevance and general background of the study. We will provide a thorough definition of PE and an overview of the global PE industry. We will also explain the difference in the allocation of PE worldwide before we narrow it down to Tanzania's PE market and the country's political and economic situation.

EVCA, (2007) defines PE[1] as "*the provision of equity capital by financial investors over the medium or long term to non-quoted companies with high growth potential*" (p. 6). Centrowski, Petro, Martin, & Wadecki, (2012) provide a similar but simpler definition, that PE is a medium or long-term investment that is not publicly traded. PE differs from the term VC, in that VC firms typically invest in young or emerging companies (Kapland & Stromberg, 2009). In this study, we use the term "*PE*" as a generic term that includes all investments in private firms. For ease of explanation, the term "*PE funds*" encompasses early-stage VC funds and late-stage funds.

The PE process starts with raising PE funds and proceeds through the investment in, monitoring of, and adding value to firms. The process continues as the PE firm exits successful deals and returns capital to its investors and renews itself with raising additional funds (Gompers & Lerner, 2001). PE firms are normally organized as limited partnerships and raise equity capital through a PE fund[2]. The limited partnerships include general partners (GP) who manage and invest the fund, while the limited partners (LP) provide most of the capital (it is the norm for GPs to provide minimum 1 per cent of the total capital). The LPs include institutional investors and are typically pension funds, endowments, and insurance companies (Kapland & Stromberg, 2009). This is illustrated in figure 1.

[1] We use PE as an umbrella term that includes venture capital, buyouts, growth, turnaround, balanced, co-investment, co-investment multi-manager, direct secondaries, PE secondaries and PE fund of funds (Preqin , 2008).

[2] "Most PE funds are "closed-end" vehicles in which investors commit to providing a certain amount of money to pay investments in companies as well as management fees to the private equity firm" (Kapland & Stromberg, 2009, p. 123).

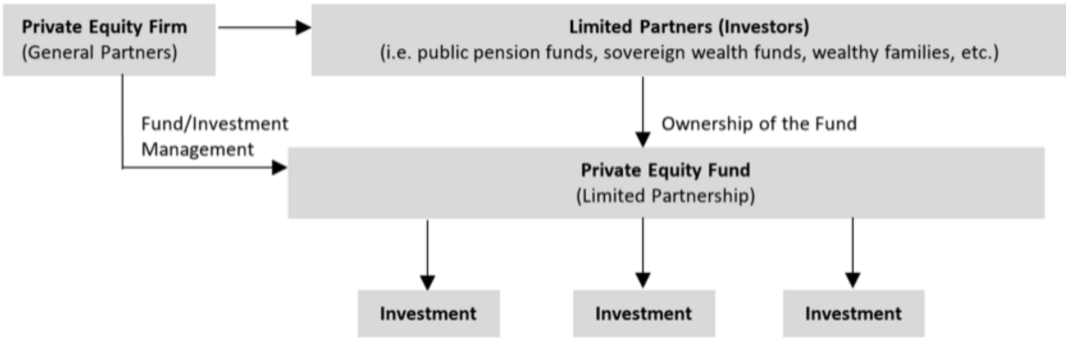

Figure 1: PE Structure (Kaplan & Stromberg, 2009)

Successful PE firms stay in business by raising a new fund every 3-5 years, whereas each fund is expected to be fully invested within five years and is designed to exit from the investment within 3-7 years (Stowell, 2018). PE investment by a fund typically last over a period of 2-7 years, and the limited partnership is structured over a 10-year horizon so that the fund manager can select investment over the first years. The investments are made with a focus on capital gains upon an exit, as entrepreneurial firms typically are not able to pay interest on debt or dividends (Douglas & Johan, 2014). Lerner, (1997) emphasizes the importance of the exit process and argues that successful exits are critical to ensuring attractive returns for investors. Traditionally, PE firms have had three options when exiting an investment: a corporate acquisition, an IPO, or a secondary deal which is selling a company to another PE firm (Gelfer & Wagner, 2014). In the case of exit preferences, it is widely accepted in PE literature that a public listing of the invested company is the ultimate and most successful form of exit (Gompers & Lerner, 2001). However, investors can also realize return upon exit through secondary buyouts or trade sales (Folus & Boutron, 2015). Moreover, PE markets in developing countries are often characterized by the presence of Development Finance Institutions (DFIs) in addition to traditional PE firms. The DFIs are typically created by governments to promote economic growth and support social development (The World Bank, 2017). This means that their motivations differ from commercial investment, as they fill an intermediary space between public aid and private investments. Nevertheless, DFIs also depend on profits from their investments to ensure long term financial sustainability (Dickinson, 2008). Their investment structure is similar to the structure of traditional PE firms, which is described above, but DFIs are often more risk tolerant and have a longer investment horizon (Dickinson, 2008).

2.1 Global Private Equity

Figure 2 shows that the total value of PE-backed buyout deals worldwide had reached its peak (762 billion U.S dollars) in the year 2007. Due to the financial crisis in 2008, the deal value experienced a drastic decline in both 2008 and 2009. However, billions of dollars have been invested by the PE industry over the last decade (Meles, Monferra, & Verdolivia , 2014). Despite the negative effects of the financial crisis, both the number of investments and fundraising activities encountered an increase since 2009 (Bain & Company, 2018).

Based on an increase in both buyout value and exits, the global PE industry showed another solid year in 2017. As investors' enthusiasm grew, the largest buyout funds in the history were raised in the US, Europe, and Asia. This resulted in increased pressure on GPs to keep the good times rolling. The increase in investments led to high competition for assets and record-high deal multiples which made it difficult to find new targets. Notwithstanding, PE funds globally faced a growth in investment value in 2017 showing average buyout deal value at 440 billion U.S dollars (Bain & Company, 2018).

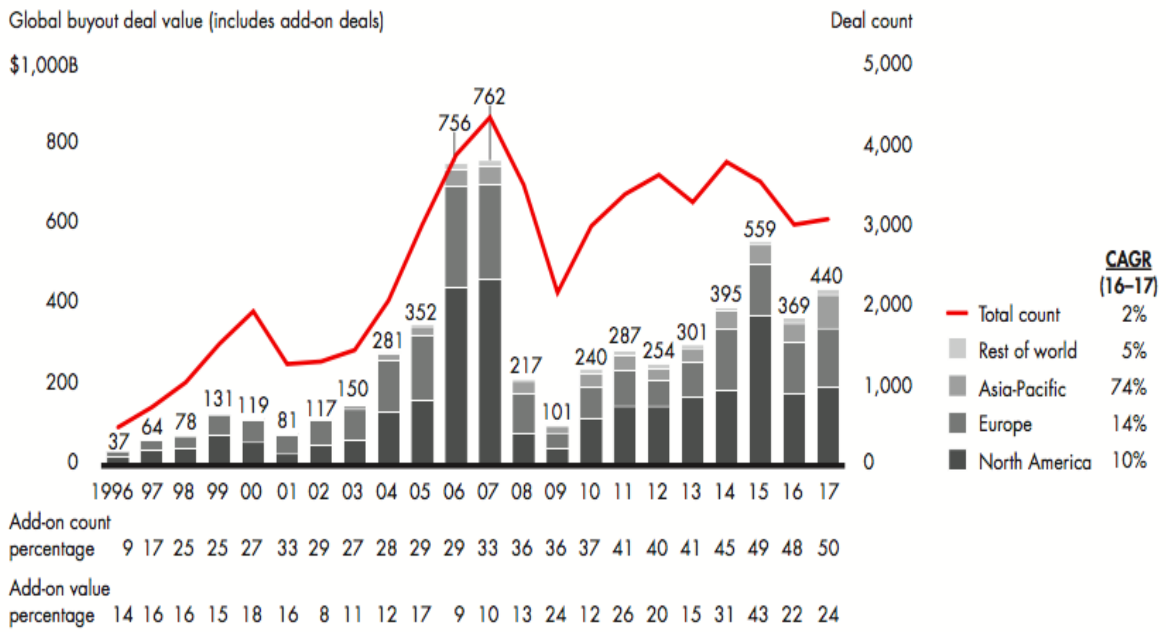

Figure 2: Global buyout deal value (includes add-on deals), 2017 (Bain & Company, 2018)

Brahamst, Bagshaw, & Kelly, (2018) acknowledge that the global PE activity is increasing, and imply that the explanation for the industry's excellent performance is based on five factors. For one, it could be attributed to exceptional returns as the PE industry delivered a double-digit internal rate of returns for investors and outperformed the stock market with good margins. According to Bain & Company, (2018) buyout funds faced high returns to equity in the US, Europe, and Asia (Bain & Company, 2018), which give motives for investors. In turn, this resulted in a mounting level of dry powder[3]. This leads us to the second factor, the fact that managers accumulated more dry powder than history has ever shown, estimated at $1.8 trillion in 2017 (McKinsey&Company, 2018). Cheap debt on favourable terms is also a considerable factor in the explanation of the industry growth. PE firms have been capable of sourcing easily accessible debt at good terms (Brahamst et al., 2018). Platt & Vandelvelde, (2018) claim PE participants are riding high on a wave of cheap debt, leading buyout values to levels not experienced since the financial crisis. To paint a picture of the extent; in about half of the deals in 2018, the PE firms were successful in raising debt equivalent to at least six times the annual EBITDA of the company they bought. Another significant factor is digitization. The use of digital technology across all industries had a positive impact on the PE industry, not only making it possible to identify trends early within a sector, but also conducting accurate due diligence. Acker, Roberts, Schneider, Naydenova, & Schreiber, (2016) back this up and argue that companies will in sum, have much greater potential for growth and profitability. The last explanatory factor is the emergence of new managers. With new managers consistently penetrating the market with new strategies, fund structures and innovative offerings, the interest of new investors increases (Brahamst et al., 2018).

2.1.1 PE Trends

The recent growth of global PE activity has caused some trends in the PE industry. Snow, (2012) discusses these trends and claims that the following four are central; specialisation, regulation, institutionalisation and globalisation. Although history shows that PE firms used to be generalists, today firms tend to specialize in specific sectors. Due to higher competition, PE firms are becoming specialized in different industries and geographies to distinguishing themselves from competitors. Favourable returns are causing firms to be more exposed to scrutiny from regulators than before, thus the expense of being a regulated entity is something firms must encounter. Institutionalisation is another trend currently affecting the PE industry. PE firms are managing a great amount of capital from large sophisticated organisations,

[3] Dry powder refers to undrawn commitment (Hotchkiss, Smith, & Stromberg, 2011). It can be described as unallocated capital (Financial Times, 2018).

pressuring them to be sophisticated in their services. Globalisation is also a major trend to be seen in the PE industry and has successfully facilitated private capital to flow across countries with little restrictions. PE firms are helping their portfolio companies become more compatible while expanding their mediate borders (Snow, 2012). Since the global financial crisis in 2008, PE firms have moved into emerging markets as they looked for more diversification within their portfolios (Preqin, 2018). Developing countries on their part benefit from private capital flow because they possess limited domestic savings, and PE capital brings with them finance, managerial skills, technology, and marketing expertise (Bank of Tanzania , 2001).

2.2 PE in Emerging Markets

While there has been a continuing increase in capital raised for the PE industry globally in the last decade, the fundraising for emerging markets[4] reached its peak in 2014 with $120bn of capital raised falling just under $90bn in 2015, and closing at $115bn in 2017 (Preqin, 2018). In the aftermath of the global financial crisis in 2008, there was a restructuring of the funds allocated to emerging markets as a way for investors to seek diversification in their portfolio. The proportion of capital raised for emerging markets on a global scale recorded its zenith year in 2011 ending with 55 percent of all funds closed, and 40 percent of capital raised going to funds focusing on the emerging markets. The most recent figures show signs that investors have regained their confidence, and again strengthening their position in the developed markets while markets in developing countries struggle to keep pace. Emerging markets are seeing a steady decline from their top year and only managed to capture a 23 percent share of the capital raised in 2017 with the most up to date statistics for 2018, predicting a drop to pre-crisis levels for capital raised in emerging markets (Preqin, 2018).

[4]Emerging markets includes all countries in Africa, Asia (excluding Hong Kong, Japan and Singapore), Central & Eastern Europe, Latin America (South and Central America and the Caribbean) and the Middle East (excluding Israel). (Preqin, 2018)

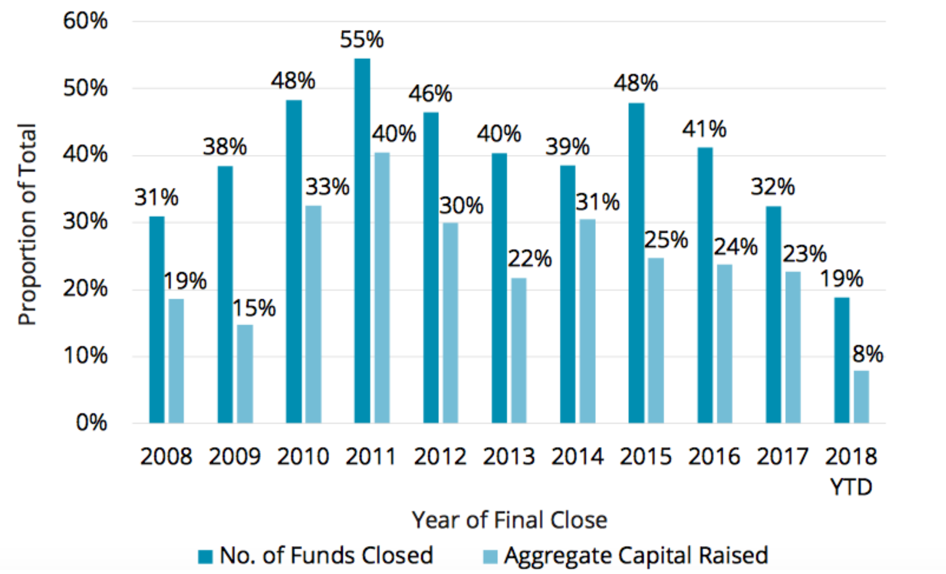

Figure 3: Emerging Markets-Focused Fundraising as a Proportion of All Private Equity Fundraising, 2008 - 2018 YTD (As at April 2018) (Preqin, 2018).

Emerging markets encompass a geographical disperse range of markets with a high level of imbalance in terms of fundraising and number of funds present in each region. Going deeper into the numbers for each region, emerging Asia represents the majority share with roughly 80 percent of the total aggregate capital raised since 2008. Latin America lost its position as the second largest contributor to the central and eastern part of Europe, after a destabilisation of the political and economic environment for several countries in that region recently. While they came in second and third, they only contributed to 3-4 percent of total capital raised posing no threat to emerging Asia as the predominant region for PE investment attention. The vast majority of funds looking at investing in emerging markets seem to prefer an allocation of their capital to one specific area (Preqin, 2018).

2.2.1 PE in Africa

Focusing on the African region, which is more aligned with the objective of this study, investors have not been overly enthusiastic by the current investment climate despite growth prospects being in their favour. Africa represents a minority share of about one percent of total PE capital raised in 2017 for the emerging markets, which has been at approximately the same level for the last decade (Preqin, 2018).

The evolution of the PE industry started in the early 1990s when DFIs entered the market. Their focus was different from that of traditional investors elsewhere as they also had a goal of economic and industrial development, and were not solely measured on the rates of profit (Dupoux, Becker, Hammoud, & Fihri, 2016). The two decades stretching from 1980 to the turn of the millennial are sometimes referred to as the lost decades, and Africa as a region was mostly ignored by multinational PE firms in that period. A downturn in the commodity prices along with several other unfavourable political factors shifted the post-independence momentum and economic growth to stagnation. It was deemed too risky, with too many uncertainties for fund managers to consider that area, and investors turned to other emerging markets to diversify their portfolio (Dupoux, Ermias, Heuze, Niavas, & Von, 2014). The DFIs led way with a greater willingness to take risks and lower levels of expected returns than traditional investors, and thus were better suited to serve the market at that time. Africa would soon after emerge from the economic stagnation, and by the start of the new century it also caught the attention of major international PE funds (Dupoux et al., 2016). An increase in commodity prices, a surge in domestic demand, and a more stabilized political climate for several countries turned the net capital flow positive after a period of capital-draining and retreat of foreign investors (Dupoux et al., 2014). Since then, the number of funds, capital raised, and the number of exits for PE investments in Africa has kept increasing on a growing wave of optimism until the recent slowdown. Before the successive record years of 2014 and 2015, there was a common belief by many investors that the African region would experience a similar growth seen in other emerging markets like parts of Asia and Latin America. The rationale for this was mainly that the rise in commodity prices combined with a more stabilized political situation, and an increased consistency in infrastructure investments, would lead to sustained growth of the economies in Africa (EMPEA, 2018).

The booming optimism amongst eager investors was slowed down by yet again experiencing the sensitivity of the market when it comes to the commodity prices coupled with policy uncertainty and increased currency volatility. African based investors adapted to the situation by adopting a more cautious approach to potential new investments, and sought for sectors and regions less affected (EMPEA, 2018). The southern region's share of PE transactions experienced a substantial decrease by 11 percent in the last decade, and the same trend could be witnessed in North Africa, with a decline of two percent. East Africa experienced the strongest growth in their share of PE transactions which is currently 3 percent higher than North Africa's after lagging behind in the previous years (AVCA, 2019; AVCA, 2015).

2.2.2 PE in East Africa and Tanzania

The east African region gained interest as the other major regions like southern and northern parts of the continent were hit by the economic downturn (EMPEA, 2018). The eastern region experienced record high fundraising and increased positivity from investors unlike other parts of the continent who were struggling with an investor retreat after the high of 2014. GDP growth for the countries in East Africa kept climbing as their economies were less reliant on the commodities whose prices plunged, particularly the oil prices, and benefited from being net oil-importing countries. In addition, the region maintained its growth momentum by escaping the worst of currency volatility and sustaining a relatively stable political climate (Deloitte, 2017).

Most of the countries in the region have experienced an increased PE activity in recent years, and continues to attract more investments. Despite the region's strong growth in PE investments, Tanzania struggles to attract investments and increase the number of PE deals (KPMG & EAVCA , 2017; The Citizen, 2018). In the period of 2007 to 2014 Kenya stands out with 54 percent of the total number of PE transactions in the region, and Uganda comes in second with 16 percent. Tanzania were only able to attract a small share and reported 13 percent of the total number of PE transactions (AVCA, 2014). For the next period from 2013 to 2018 both Kenya's and Uganda's shares increased to 58 percent and 19 percent, respectively, while Tanzania's share lags behind and reported a decrease to 9 percent (AVCA, 2019). The same trend is observed for the value of Foreign Direct Investment (FD)[5] in Tanzania, which have decreased continually after the peak in 2013. The value of the inflows was almost halved in 2017. This contrasts with the long period of steady growth in investments from the mid 90's to 2013, and the country's continuing strong growth in GDP (The Global Economy , 2017).

[5] FDI are the net inflows of investment to acquire a lasting management interest (10% or more of voting stock). In an enterprise operating in an economy, other than that of the investor. It is the sum of equity capital, reinvestment of earning, other long-term capital and short-term capital as shown in the balance of payments (The Global Economy , 2019).

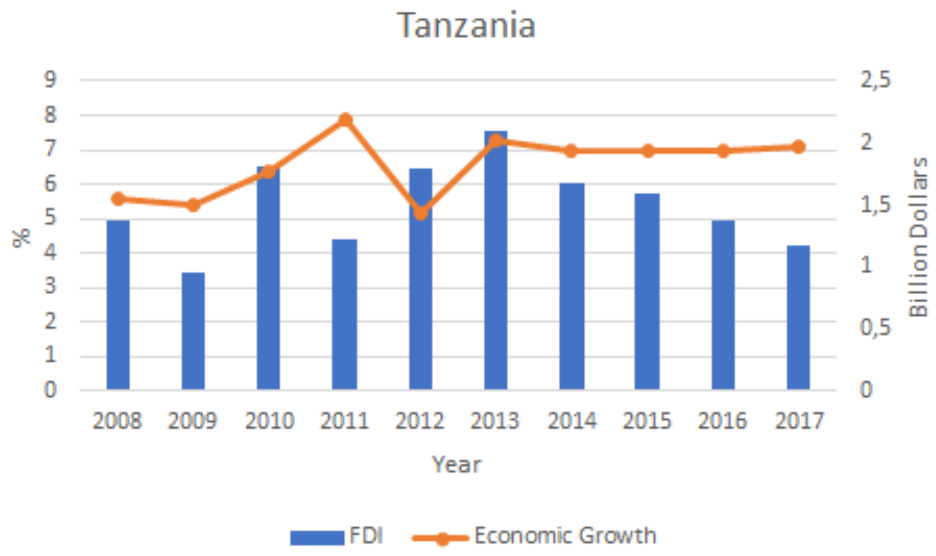

Figure 4: Economic Growth & FDI, Tanzania (The Global Economy, 2018).

2.3 Political Economy of Tanzania after Independence

Tanzania has since its independence from Britain in 1961, enjoyed a more stable political climate than its neighbouring countries in East- and Central Africa. The Chama Cha Mapinduzi (CCM) party has been the dominant power in the political landscape since Tanzania gained its independence, with all five of the presidents elected being a member of their party (Anyimadu, 2016). After being a single party state until 1995 with free elections, it introduced political pluralism and since then, multiparty major elections every fifth year. CCM continued to win the presidency and got the majority of the seats in the parliament with their latest president Dr John Pombe Magufuli being elected in 2015 (Ngowi, 2009). Despite the country's reputation for stability and peace, it has experienced major shifts in political direction and policies since the British colonial era, leading up to the current situation of the country. Ngowi, (2009) divides the economic development and change into three distinct time epochs that he mainly attributes to the political leadership.

The first epoch, lasting from 1961 to 1967, started when Tanzania gained its independence, but was characterized by the lasting presence of the colonial masters and Asian businessmen in the economy. The new Tanzanian government led by TANU, who later formed the CCM together with Afro Shirazi party from Zanzibar, continued with a market-oriented approach with private sector capitalism as it had been in the colonial days. The extension of the policies after the independence did not produce the desired outcome for the Tanzanians, as poverty continued to dominate, and it caused a lot of imbalances as state intervention could not avoid several market failures. The interests of the former colonial power and foreign stakeholders were still strong while the local Tanzanians experienced few benefits from the capitalistic market approach (Ngowi, 2009).

During the first six years, the investment climate was very favorable, especially for foreigners, but the country did not experience the post-independence development that it had expected. This leads us to the second epoch, which both Cooksey & Kelsall, (2011) and Ngowi, (2009) refer to as a big turning point in Tanzanian history when there was a political decision to adress the imbalances that later culminated in the well-known Arusha declaration. This declaration named "Umajaa" stated that the country would change its market-oriented economy and follow more socialist-oriented economic and political policies. The state began to intervene and take control over important means of production and established parastatals that marked the end of an era of privatization and a passive government. The conditions for private sector entrepeuneurs and people who wanted to invest in businesses were rough, with very few incentives in contrast to the previous epoch. The government imposed trade controls and both import and export fell, while the domestic production suffered from severe inefficiencies due to the government policies that led to state monopoly in several industries. Social services like education and health were key areas that the government focused on, and contributed with services that was almost fully subsidized which made them available for a much larger part of the Tanzanian population (Ngowi, 2009).

This era left behind huge investments in human capital, in particular, investments in education from primary to tertiarty level, which are viewed as a positive contribution and a foundation for the economic and social development for the country in the time ahead up until today. The last epoch, Ngowi, (2009) recognizes and names reform era, started in the midst-1980 when they returned to a more capitalistic market approach. There were several major reforms that initiated the economic liberalizition such as opening up agricultural markets, decreasing the control over foreign exchange, and reducing consumer and social service subsidies (Eriksen, 2018). Investors gained confidence, and more capital started to flow into private sector businesses after a period of capital-draining from important industries. This was further followed up by a new series of reforms that would provide more incentives for investors, as trade and foreign exchange control for businesses were eased, price controls schemes abolished and the number of parastatals were decreased (Cooksey & Kelsall, 2011). This process and approach have been continued by the everlasting political leadership of CCM with a focus on economic measures instead of the Umajaa's period of social measures on development (Knippels, et al., 2017).

2.4 Current Political Economy of Tanzania

The economy of Tanzania has over its course of nearly 58 years since its independence experienced numerous ups- and downturns together with its changes in policies. The most noticeable was perhaps the economic collapse from 1979 to 1985 that ended the "Ujamaa" period with a socialist-oriented economy (Cooksey & Kelsall, 2011). From the start of the year 2000, Tanzania has been one of the countries in Africa with highest GDP growth and also compared to any previous period in Tanzania's history, the growth has been exceptional (Potts, 2005). At the same time, we witnessed very strong growth in FDIs into Tanzania which had been almost negligible in the past. This growth in investment ended with a downturn in 2014, one year before the presidential election and has continued downwards since then. The Bank of Tanzania also reports a similar trend in their 2016-2017 report for private investment, in contrast to the growth in GDP which did not slow down in this recent period (World Bank, 2018).

In the time around and after the election of the new president Magafuli in 2015 there has been a change in investor outlook (The Economist , 2018). The new government has prioritized raising revenues, hiring of domestic workers in businesses, and protection of local and domestic industries. This has resulted in new and more aggressive tax collection systems for the most profitable industries, difficulties for foreigners getting work permits, and increased trade control (EB, 2018).

In the 2019 index of economic freedom by the (The Heritage Foundation , 2019), Tanzania is ranked as the 94th freest country overall, but when splitting up the index and comparing it to previous years we get a better picture of the situation. In the period since 2015 there has been a slight improvement of the overall score driven mainly by judicial effectiveness, fiscal health and government spending offsetting the negative change in trade-and investment freedom. In addition, the index characterizes business freedom as repressed, and this picture we get is in line with what investors point out to be factors of concern (The Economist , 2018).

The new government intends to focus on the private sector, industrialization and increasing employment. However, there is a growing concern for the business environment in the private sector and changes in policies have made the long-term prospects for investment less reliable (The Economist, 2017). According to The Heritage Foundation, (2019), abrupt tax increases, erratic regulatory changes, uneven policymaking, rising protectionism, and lack of transparency represents the concerns of investors and deter private investment.

The increased and spontaneous interventions from the government into economic regulations includes price controls on certain commodities, trade protectionism, and inefficient regulations that make it costly to launch new businesses (The Heritage Foundation , 2019). The interference in the market has made many doubt the government's attitude toward market principles, and showed the weakness of the institutional economic framework. The government still controls pricing in large sectors such as agriculture, telecommunications, banking, energy, and transport despite that many of the state-owned enterprises were privatized. The government's recent interference in the agriculture sector in particular, combined with the increased protection of domestic industries has caused concerns for investors in the private sector (Bertelsmann Stiftung , 2018). To protect local industries there has been a use of increased tariffs and import- and export bans, but these policies have not proven to be effective in developing these industries domestically as planned (EB, 2018). According to The Heritage Foundation, (2019) trade- and investment policies needed to sustain open markets, are undercut by government interference in the economy. In addition, there have been implemented labour- and immigration regulations that have made it more difficult to hire foreigners, these are regulations that require employers to attempt to employ Tanzanian citizens before seeking foreign expertise. There are also restrictions on the number of expatriates possible to recruit for foreign investors that limits their ability to bring in the desired skills and competence.

In 2016, the new government prioritized raising revenues, which resulted in new and more aggressive tax collection systems for the most profitable industries (EB, 2018). This campaign to raise revenue and the tax collection was perceived as arbitrary and harassing, making investment less attractive in recent years (EB, 2018). The strict controls introduced to improve tax discipline and the implementation of new taxes increased uncertainty among investors, and were viewed as erratic and unpredictable. These changes have undermined investor's confidence and increased the risk of contract alteration in Tanzania (JLT , 2018). Although greater emphasis on tax discipline is desirable for the development of the country, the policies and methods were considered unfavourable for the business environment because of its inconsistency and biased targeting (Bertelsmann Stiftung , 2018).

According to the (EB, 2018), investors also expressed concerns over new laws that have been implemented without stakeholder consultation. Primarily, the laws restricting the use of international arbitration for the settlement of disputes, and the parliaments unilateral right to rewrite contract terms in cases where it is undefined raised concerns. The new laws have especially affected sectors dealing with natural resources and made investors more reluctant towards large sectors such as mining, and oil and gas (ALB, 2018). The risk of investing in these sectors has increased as a consequence of the new laws, due to investors lack of trust in a fair settlement. The new demands from the government to resolve disputes in Tanzanian courts make investors worried that the government gains an advantage, and that the process will be inefficient and time-consuming (EB, 2018).

The country continues to benefit from a relatively stable political climate compared to its neighbouring countries. However, increased restrictions on political activity and a growing opposition has questioned the country's ability to sustain its stable political climate. Tanzania experiences a period where it exists a significant political opposition that poses a threat to the ruling party for the first time in history as an independent nation. The government has responded to this by limiting the possibilities to engage in political activities for opposition parties and civil society organizations. There have been introduced restrictions to debate issues publicly and peacefully assemble as a way of curtailing opposition activities (The Economist , 2018). Moreover, laws to control the media and information sector were implemented by the new government which have been perceived as repressive and led to several arrests and criminal charges under the new cybercrimes act. These actions, together with several killings of local government officials, police officers, and politicians have created a culture of fear and raised concerns about emerging authoritarian tendencies (Bertelsmann Stiftung , 2018). The recent changes in the political environment could affect the future stability of the country, which makes investors uncertain of the consequences for the business environment and potential investment opportunities.

Widespread corruption and a fraudulent culture, which have been embedded in societal-, economic-, and power relations, have long been a challenge and a burden for the country (Heilman & Ndumbaro, 2002). However, the new president has introduced an aggressive anti-corruption campaign that has led to an increased judiciary budget, new corruption cases, and a decrease in perceived corruption. Moreover, the government's agenda to fight corruption has taken measures to end the culture of impunity, making government officials more reluctant to engage in corrupt activities. Despite the new government's focus on battling corruption and illicit practices, corruption is still considered to be a major problem in Tanzania, and remains a concern for many investors. In particular, investors face difficulties with corruption in government procurement, privatization, taxation, and customs clearance (EB, 2018). The Transparancy International, (2018) Corruption Perception Index shows that the general public perceives that the level of corruption has declined in recent years, but Tanzania continues to perform poorly and is ranked 99th of 180 countries listed.

Although Tanzania continues to experience a steep growth in GDP, the level of investment activity has not been following the same pattern. After a period of optimism and increased activity from investors, there has been a decline in investments where the change in investment activity and outlook seem to be related to the new government and changes in policies after the 2015 presidential election. Tanzania is a country that has one of the highest economic growth rates among its peers in the region, and great potential with an abundance of natural resources, still, the country seems to struggle to attract investments. This study aims to understand and explain the key factors that drive the level of investment activity and affect the investment decision in the case of Tanzania, with a focus on the PE market. The next chapter provides an overview of existing theory and literature on what determines the development of PE markets.

3. Theoretical Background and Literature Review

3.1 Theoretical Background

In an increasingly globalized world where physical distances become less important, especially in the world of financing, PE firms look to new markets for opportunities. Possibility to geographically diversify and exploit opportunities in different parts of the world and markets with less history of PE financing, means that an important step in the allocation process is evaluating the risks associated with entering the new market. This creates a stronger need for an overall assessment of the socio- and macroeconomic factors of the new market. In order to assess the attractiveness of different markets, it would make sense to incorporate the factors similar to those included in a PESTEL framework for an overall analysis initially. The PESTEL framework is introduced to provide a deeper understanding of the overall macroeconomic business environment and the determinants of the PE markets presented in the literature review. The VC and PE Country Attractive Index (2018) is based on external socio-economic and environmental factors similar to those in the PESTEL framework, hence this chapter starts with a brief presentation of the PESTEL analysis.

3.1.1 PESTEL

PESTEL is a tool used to strategically evaluate the impact of several factors that might affect business investments. The analytical framework helps an organization consider the external environment before taking on a project so that potential risks and issues are captured upon investment (Rastogi & Trivedi , 2016). PESTEL stands for political, economic, social, technological, environmental and legal factors. As Roos, Krogh, & Roos, (1996) express, the strategical analysis can be helpful in several ways; as a tool for identifying key factors in the environment which affects the firm, detecting changes in the environment, and disclosing how these changes might affect the business.

Political: These factors determine the extent to which a government in the hosting country may affect the respective economy or industry. Changes in the political environment can have significant effects on the business environment, and may include changes in the domestic political climate, government change, and specific legislation and regulation (Gupta, 2013). Haberberg & Rieple, (2008) reason that such factors affect the stability of an industry, and are important to consider since uncertainty makes it more difficult for managers to develop long term strategies.

Economic: Factors of the economic environment are concerned with the costs for the organization, and are the determinants of the economy's performance that directly influence a company (Rastogi & Trivedi , 2016). From an economic perspective, it is easy to see that businesses and the economic environment are closely connected, thus it is highly important to identify critical economic factors since it determines the future of the business. For instance, all products and services are either purchased by consumers or government departments that are funded by taxes and duties, making consumer spending power (and factors affecting the spending power such as economic growth, unemployment, and interest rates) a major factor in the prosperity in any given industry (Haberberg & Rieple, 2008).

Sociological: The sociological features contemplate all events that affect the market and community socially, referring to cultural expectations, norms, population dynamics, and global warming (Rastogi & Trivedi , 2016). An example of this can be consumer taste, which can vary in geography, demography, and income level. Consequently, a good environmental analysis needs to take relevant trends, such as economy booms and busts, into account.

Technological: These factors capture technology and innovations in technology that affect the operations and business environment for a firm. Technology can influence both the market and industry for a firm in different ways as a barrier to entry or serve as a possibility for competitive advantage when examining the external environment. It is distinguished by its often rapid and constant change in the ways it affects the business and its surroundings, that could be crucial for a business to pay attention to (Rastogi & Trivedi , 2016).

Environmental: According to Rastogi & Trivedi, (2016) environmental factors are those influenced or determined by the surrounding environment. These factors are often linked to other factors included in the PESTEL, and might affect the business in various way through them. Environmental factors could strengthen their impact on industries and markets or be exploited or resolved by other factors. For example, the interaction of technology and environmental factors like climate and health work in a two-way direction, by creating awareness of problems and possible solutions (Haberberg & Rieple, 2008). Thus, for a business gathering information of their external environment it is important to notice possible links between the factors when planning their strategy.

Legal: The legal aspects affecting the business environment can vary significantly between countries and markets, though often not changing as fast as other factors. These factors include laws on labour, trade restrictions, taxation, and consumer laws among others which work both on the internal and external environment for businesses. An analysis of the legal environment must consider all aspects that could affect the operations of the business. Especially before entering a new market these factors will be critical to assess, as certain legal aspects could differ substantially. Differences and changes in laws and regulations could pose threats to a business that could alter their operations in ways that make it difficult to be profitable. A critical assessment of this is fundamental for an analysis of the business environment when developing a strategy (Rastogi & Trivedi , 2016).

The PESTEL analysis is advantageous in identifying external factors affecting a certain business or industry, which is an important part of the process for institutional investors' allocation decision. There has been a growing body of research focusing on the factors that attract PE investments and why some countries have a large and vibrant PE market while others struggle to attract investments.

3.2 Literature Review

Despite a large number of studies, there still exists no broad consensus among the researchers on what determines that some countries are able to attract more risk capital than others. Several studies have addressed the importance of the socio-economic environmental factors in both developed countries with an established PE market and emerging markets with a lower presence of institutional risk capital investors. Most of the literature that attempts to answer what features in the macroeconomic environment best facilitates, and attract PE investments at aggregated country levels, suggest a quantitative approach to determine the importance of the factors. There also exists a number of studies that, within the spectrum of the external environmental factors, try to isolate subsets of the main components as explanatory variables to answer the question.

3.2.1 Global PE

Groh, Liechtenstein, & Canela, (2008) examine the drivers for institutional investors in the process of allocating risk capital to markets globally. They aim to rank the importance of several decision parameters using a questionnaire targeting limited partners on a worldwide scale. Based on answers from 75 investors that rank each decision parameter on a seven-point Likert scale, they apply several non-parametric tests to analyse the data and determine the rankings. Their findings reveal that the protection of property rights is the main concern for investors when allocating their capital. They also stress the necessity of finding local quality GPs and skilled management teams. Finally, when making decisions about country allocation the expected deal flow and investors fear of bribery and corruption are also issues of significant importance.

3.2.2 PE in Developed Countries

Precup, (2015) studies the evolution of PE investments across Europe during the last financial crisis while analysing and identifying the determinants of the European PE market. Utilizing an empirical panel data analysis of 27 European countries in the period 2000-2013, the study investigates seven different macro determinants and their effect on the development of the PE market. The findings reveal two main drivers of the PE activity in Europe; market capitalization and unemployment. The market capitalization had a statistically significant positive effect, while unemployment showed a significant negative impact on the PE market, in line with the proposed hypothesis and previous literature. Furthermore, the study found the level of corruption and productivity to be relevant in explaining the development of PE activity. The negative impact of corruption and positive impact of productivity were also as expected. The last significant determinant in the study, economic growth, surprisingly revealed a negative relationship between the growth of a country's economy and the level of investment. The independent variables; interest rate and research and development expenditures did not have a significant effect in this study.

Bernoth & Colavecchio, (2014) conduct a similar study where they divide the macroeconomic determinants into four categories, and define a number of subsets for each component based on previous literature. The main group of factors include economic environment, financial environment, labour market environment, and political, legal, and social environment and the factors have 42 different subsets in total. After collecting data from 16 different countries across Europe for the period 2001-2011, they split up the numbers into two groups; Central- and Eastern Europe (CEE) and West Europe. They then apply a test for robustness of the determinants and only include the robust variables in a fixed-effect panel estimation. In line with the study by Precup, (2015), the findings show a negative relationship between GDP growth and the level of PE investments in CEE, but find a significant positive relationship in the sample for Western Europe. This study also confirms the positive effect of market capitalization, but their findings of a positive impact of the unemployment rate for western European countries contradicts the findings of Precup, (2015). In addition, they emphasize that political stability and regulatory quality have no significant effect on PE investments for CEE, but surprisingly they show a significant negative relationship for Western Europe. This implies that politically unstable countries with unfavourable business conditions attract more PE investment.

Analysing factors affecting the early-stage development of the PE markets across a group of nine developed countries from 1985 to 1999, Kumar & Orleck, (2002) conclude that PE development varies significantly even among the most developed countries. Similar to Precup, (2015) and Bernoth & Colavecchio, (2014), they point out that market capitalization is an important explaining factor. They have also tested the effect of the cost of capital and legal systems, and argue that they both are significant in determining the differences in PE allocation. In addition to the mentioned variables, market transparency and patents denied are both significant determinants of the PE market in the period 1996-1999, which are an indicator of the increased importance of transparency as PE markets develop. It is confirmed in recent years with increased globalisation and competition that transparency becomes vital for the understanding of new markets and industries (PWC , 2013).

Previous work that solely focused on the VC markets for the developed countries extends the line of conflicting conclusions. Felix, Gulamhussen, & Pires, (2007) and Jeng & Wells, (2000) find that GDP growth is not statistically significant while Gompers & Lerner, (1997) suggest the contrary, that GDP growth has a significant positive impact on investment levels. Furthermore, Felix et al., (2007) reveal that market capitalisation growth shows a positive effect in the data set, in line with the study by Gompers & Lerner, (1997), while Jeng & Wells, (2000) obtained no significant relationship between market capitalization growth and VC investment in developed countries. In addition, Felix et al., (2007) find interest rates, the unemployment rate, IPO divestment and trade sales divestment to be significant determinants of the VC market. Gompers & Lerner, (1997) conclude that capital gains tax rates are a significant determinant. Jeng & Wells, (2000) discover that the total market value of IPOs has a positive effect on late-stage VC investments while labour market rigidities negatively affect early-stage VC investments.

These studies sum up some of the important findings from research focusing on PE development in markets with the most history and biggest share of the PE investments globally. Even though there is a large body of existing research, it does not point us in a clear direction to decide which factors that make these countries attract the most PE investments. Other studies try to offer answers for the large differences in risk capital allocation by focusing their attention on the factors affecting emerging markets ability to attract PE investments.

3.2.3 PE in Developing Countries

Adrian, (2014) compares the drivers for the PE markets across six countries in emerging Asian and 15 developed countries from 2000 to 2011. Looking at the developed PE markets, the major determinant of funds raised seem to be the amount of credit provided by the banking sector, exit opportunities in the form of IPOs, and R&D expenditures. For the emerging markets, the study shows that the time required to start a new business, and costs related to starting a business are important determinants for the overall PE development. The study also shows, in contrast to developed countries, that market capitalization plays a significant role in explaining the level of investment in emerging countries. Lastly, he finds a negative relationship between credit provided by the banking sector and funds raised opposite from the findings for the developed countries.

Oino, (2014) investigates the macroeconomic and environmental determinants of PE investments in nine Asian countries using a dataset spanning from 2004 to 2013. He applies extreme bounds analysis to test for robustness, and finds that corporation tax rate, GDP growth, disclosure index, and investors protection are robust variables. In addition to the robust variables, he identifies six variables that are likely robust; inflation ratio, stock market value, property right index, lending rate, legal costs, and time in days to start a business. The implications of the study are that fast-growing economies, well-developed stock markets, and robust legal systems are more likely to attract PE investment. A study focusing on 36 countries in Africa by Adongo, (2011) tries to identify the determinants of VC activity using a cross-sectional dataset. The results show that rule of law, R&D expenditure as a percentage of GDP, better information between investors and potential investees are positively and significantly related to VC activity in Africa, while Capital gains tax rates have a negative impact. Similar to Adrian (2014) this study emphasizes R&D expenditure as an important factor, but suggest further research to determine the direction of causality between innovation and VC investment.

Oni, (2017) studies the variables that influence VC supply in Sub-Saharan Africa by comparing eight countries in the region, and using data from the period 2006 to 2015. The results indicate that there is a significant positive relationship between IPOs and market capitalization, and VC investments. The remaining variables estimated, unemployment rate, FDI inflow, and trade openness do not have a significant impact in the study. It is argued that the Sub-Sahara African governments should focus on improving infrastructure, corporate governance and develop their equity markets in order to attract more capital investments.

There is an absence of research focusing on determinants of the development of the PE market in Tanzania, but there exists some literature which examines the determinants of FDI in Tanzania. As FDI includes many of the same aspects as PE does, it requires an external analysis of the investment climate. Hence, this should give us an indication of which factors contribute to a favourable investment climate. A study by Shawa, (2014), utilizing data from a period of 33 years, analyses the relationship between FDI and its determinants in Tanzania. The main conclusion of the research is that market size, infrastructure development and natural resources availability are the major determinants of FDI inflow to Tanzania. Surprisingly, the results found that natural resources availability had a negative impact on FDI.

Mfinanga, (2018) also seeks to explain the determinants of FDIs from 1990 to 2015 in Tanzania. The study suggests that there are two key drivers for the development of FDI. First, the results show that the exchange rate is a significant determinant indicating that the flexible exchange rate policy increases the inflow of FDI in the country. Second, the market size was found to be a significant explanatory variable with a negative sign implying that the small market size in Tanzania discourages the inflow of FDI in the country.

It is important to notice that both studies of FDI in Tanzania point out their limitations in the inclusion of variables that might have contributed to explaining the development of FDI. They suggest that further studies should include variables such as labour cost, taxation, political stability, and education level in order to ensure exhaustion of the variables that in turn can improve the validity.

Particularly for emerging markets, there is a lack of historical data and statistics that makes it challenging to check for and test all the possible socio-economic and institutional determinants with a quantitative research framework. Despite of the importance of DFIs in the early-stage development of markets for risk capital in developing countries, most of the literature on determinants of PE markets in developing countries does not distinguish, nor highlights potential differences between drivers of traditional PE and DFIs. A reason for this might be that DFIs, despite of differences in motives, to some extent also seek profit and a favourable investment climate similar to traditional PE firms.

For the case of Tanzania, there exist a limited body of research on this field, thus we have included studies that discuss the determinants of FDI. The studies of selection criteria for FDI includes many of the same variables as in the literature of PE, but it is important to acknowledge the small set of factors included, and the difference between the two forms of investment. Some countries might be able to attract a large amount of FDI, but have a poor market for PE investments (Ptacek, Kaderabkova , & Piecha, 2015). In other words, the factors that account for differences in FDI might not be reliable for differences in PE markets. The lack of research history and a theoretical foundation has affected the studies, but there has recently been made some effort to compile the literature, and create a measure that strategically evaluates the impact of several components.

3.3 Country Attractiveness Index

Groh et al., (2018) have developed a framework to rank a country's attractiveness for investors in the PE asset class. They include six main socio-economic components based on previous research that covers a broad area of importance for a country analysis. The framework serves as a guide to benchmark different countries' attractiveness from an institutional investor's point of view. The chosen selection criteria share a common feature that enables them to be quantified directly or estimated through proxies which Groh et al., (2018) present as a country attractiveness index. The six key drivers, including their subsets of criteria which are assessed in order to aggregate the index, and how they are expected to shape the national PE market are presented below.

3.3.1 Economic Activity

Groh et al., (2018) argue that a country's economy affects the national PE market and expectations of growth require investments, and provide a rationale for investors to enter a market. If the economy is experiencing rapid growth, then there may be more attractive opportunities for entrepreneurs to start new businesses. Hence there are more investment opportunities for PE investors (Gompers & Lerner, 1997). The size of an economy and employment levels serve as proxies for prosperity and the overall entrepreneurial activity, thus affecting the expected PE deal flow in a country (Groh et al., 2018).

The size of the national GDP and the expected real GDP growth is often interpreted as measures for a country's economic activity. Groh, (2009) emphasizes the positive relationship between the size of an economy's GDP and the level of PE investment. For instance, the United States attracts most of the PE investments globally and have the largest GDP, while developing countries with the smallest GDP seems to attract the least investment flows. There are however exceptions to this, whereas large economies like China lag behind on PE activity, or smaller economies like Israel are able to attract a relatively larger share of PE investment compared to their GDP. The expected growth of GDP seems to be what attract many investors to less developed countries and is linked to increased investment opportunities (Gompers, Kovner, Lerner, & Scharfstein, 2008). Fast growing economies could represent opportunities for high returns for investors with a higher willingness to take risk, or be included to diversify their risk capital investment portfolio. Oino, (2014) finds supporting results in his study, where expected GDP growth is an attractive factor for investors especially in emerging markets. Bernoth & Colavecchio, (2014) confirm the cyclical nature of PE investments, and suggests a positive relationship between both the size and growth rate of GDP for western European countries and the level of investments. There might also exist a two-way causality where PE could stimulate and affect economic growth like Gudiskis & Urbsiene, (2015) show in their study.

The employment level is another factor of economic activity that could shape the national PE market across countries. Precup, (2015) highlights how important it is for policymakers to deal with low employment levels as investors seem to be susceptible to high unemployment levels. On the other hand, the findings of Bernoth & Colavecchio, (2014) show that the unemployment rate appears to play a significantly positive role in PE investment decision. An explanation for this could be that there are greater incentives for entrepreneurial activity if it is difficult to enter the labour market.

3.3.2 Depth of Capital Market

Cassar, (2004) argues that one of the most fundamental questions for start-ups are how the enterprises are financed. Black & Gilson, (1998) differentiate two types of capital markets that affect PE decisions: stock market-centred and bank-centred markets. They highlight the need for an exit strategy by the fund from its investment and argue that a well-developed stock market allows for IPO exits, and are determining in a vibrant PE market. Investors can also realize return upon exiting the deal through a secondary buyout; the sale of the company to another PE firm, or trade sales (Folus & Boutron, 2015). Groh et al., (2018) share Black & Gilson, (1998) point of view, and use liquidity of capital markets to determine how developed a country's PE market is. Moreover, Black & Gilson, (1998) reason that a well-developed stock market is an indicator of M&A market size which spurs and rewards entrepreneurial spirit as well as offer the possibility of deal sourcing and divestments.

Capital markets play a significant role in economic development by accumulating domestic savings and mobilizing foreign capital for productive long-term investment. Nevertheless, capital markets in many emerging markets remain underdeveloped or are non-existing (Bruno & Drexler, 2016). Despite their monetary nature, both credit and debt have a significant effect on real economic development (Wächter, 2012). Arguably this means that the easier it is for start-ups to get financing, the more investment opportunities there will be for PE firms. However, history shows that start-ups and young companies have experienced difficulties receiving financing from banking institutions, as they rule out firms with short operating history due to uncertainty around their creditworthiness (Gompers & Sahlman, 2002). Going deeper, Floros & Sapp, (2012) argue that banks-centred capital markets do not manage to produce efficient institutions that support PE investments. In comparison to banking markets which are conservative toward investing, a deep and liquid stock market make risk capital thrive because it directly reflects the returns to investors. Black & Gilson, (1998) affirm this and argue that in a bank-centred capital market the conservative approach to lending, as well as the social and financial incentives penalise entrepreneur's failure more than in a stock-centred capital market.

Another disadvantage with banking institutions is that debt can be extremely expensive because of compounded interest, for instance, it varies from 17 to 40 percent in Tanzania per year (Olomi & Mori , 2015). In turn, the level of interest rates in the economy could affect the demand for PE. Rising interest rates lead to PE financing becoming more attractive compared to credits of other nature, thus leading to a higher amount of PE capital being provided in the economy (Gompers & Lerner, 1997). In emerging markets, SMEs face a tremendous challenge of raising capital and experience access to affordable long-term finance to be one of the most significant barriers to the development of SMEs. Therefore, Olomi & Mori, (2015) indicate that inaccessibility of debt can point towards increasing demand for PE investments.

3.3.3 Tax Incentives and Administrative Burdens

The level of taxation and taxation regime can differ significantly between countries, even for countries in the same region (Wright, Gilligan, & Amess, 2008). PE funds invest in businesses who are subject to different kinds of taxes, but the fund itself only works as a pass-through entity. That is, all items of income, gain, and loss or expenses earned or incurred are passed on to the partners of the fund (Knoll, 2008). The complex nature of taxation and all elements that are subject to different kind of taxes, depending on time frame and location, could make it difficult for investors to consider all options and choose the most favourable. Chikaonda, (2012) shows that investors prefer markets where it is possible to create efficient tax structures that allow for a structure of the fund such that they avoid multiple taxations and minimize the tax burden. Groh et al., (2018) point out that is not straightforward to create a link between the level of taxation and the level of PE investments. Countries that seem to be most attractive for PE investments are likely to have a higher tax rate related to investments than countries with smaller PE markets.

Gompers & Lerner, (1997) and Oino, (2014) find that investors respond negatively to a high capital gains tax rate. Bruce & Gurley, (2005) emphasize the link between tax and entrepreneurial activity. They show that a lower marginal tax rate for income tax provides incentives for entrepreneurs and result in increased start-up activity. The administrative burden for businesses and time spent on tax issues might affect the entrepreneurial activity negatively. Groh et al., (2018) point out that there are many considerations regarding taxation that might shape the PE market directly or indirectly. The literature is not consistent, and it might exist different links for different investors and markets. There is evidence from studies that favourable taxation regimes for investors, especially with regards to capital gains and policy consistency, are positively related to the level of investment. Then again, we experience countries that struggle to attract investments have substantially lower taxes than more developed markets (Groh, 2009).

3.3.4 Investor Protection and Corporate Governance

In their framework for the country attractiveness index, Groh et al., (2018) argue that legal structures and the protection of the property rights influence the shape of the national PE market. In a study of differences in the capital market size, La Porta, Lopez-de-Silanes, Shleifer, & Vishny, (1997) show that countries with weaker investor protection, based on the character of legal rules and quality of law enforcement, have smaller and narrower capital markets. They discuss how a good legal environment protects potential investors against the expropriation of their assets by the entrepreneurs and increase their willingness to invest in securities, thus extending the scope of the capital market. Furthermore, La Porta, Lopez-de-Silanes, Shleifer, & Vishny, (2002) argue that low protection of property rights and minority shareholder rights could result in a higher cost of capital and lower firm valuation. Kumar & Orleck, (2002) examine the effect of both the cost of capital and types of legal systems, and demonstrate that they are significant determinants of PE allocation.

Klonowski, (2013) emphasizes the importance of local governments effort in providing institutional and administrative support to the private sector. He shows that legal infrastructure and convergence toward international accounting standards are major determinants for the development of PE markets. Cumming & Walz, (2004) extend the work and confirm that legal framework and accounting standards also determine the return for PE investments across countries. Adongo, (2011) focuses on the VC markets in Africa and finds that the quality of the rule of law, including contract enforcement and the degree of confidence the agents have in the rules of society, are associated with more developed markets for VC. Transparency in accounting and transactions were also linked to the attractiveness of the markets for investors as it has the potential to reduce uncertainty when allocating capital to less developed markets.

The literature illustrates the importance of the quality and structure of the legal system. The institutional support and legal enforcement reduce the costs for investors and could lower the barriers related to distance and differences of markets. PE investments represent a long-term relationship with its stakeholders, and this increases the importance of a stable regulatory framework and the quality of institutions.

3.3.5 Human and Social Environment

The importance of human capital relates to the need for talented and competent management teams for PE firms and the investees. The social environment includes labour market rigidities and bribery and corruption. Groh, (2009) shows that investors rely on the skills and quality of the GPs, and that the fund managers make an investment decision based on the skills of the entrepreneurs. They find that skills of GP's and entrepreneurs are ranked among the most important selection criteria for investors focusing on emerging markets. The language and cultural differences do not seem to be a major barrier, while fear of bribery and corruption seem to be influencing investors allocation decision. According to Schertler, (2003) the level of VC investments is positively related to the human capital endowments. Further, it was emphasized that venture capitalists are actively involved in monitoring and supporting the enterprises after investment, which make it a more expensive form of financing. Therefore, it is expected that VC firms are highly selective and seek businesses with the most competent management.

Black & Gilson, (1998) discuss the cultural differences as a determinant for the level of VC investments based on willingness to take risk, which lead to increased entrepreneurial activity, and in turn, increase the need for early-stage capital. Jeng & Wells, (2000) find that labour market rigidities have a negative effect on early-stage investments as it could make it costlier and more time-consuming, and lower the level of start-ups which creates less deal flow. On the other hand, Bernoth & Colavecchio, (2014) argue that unemployment has a positive effect on investments through increased incentives for self-employment if labour market restrictions cause increased unemployment. Moreover, Djankov, La Porta, Lopez-de-Silanes, & Shleifer, (2002) demonstrate that heavier regulation of business entry is associated with larger unofficial economies, bureaucratic delay, and corruption, especially for countries with lower levels of income. The study also shows that these barriers often relate to countries with less democracy and increased practice of government interventions into the private sector which could further damage the market development.

The surrounding human and social environment create different barriers or support functions for businesses and investors which affects them in various ways. It influences both the activity and development of markets interchangeably, and it could make it hard to distinguish robust factors for all markets. That said, most of the studies reviewed confirm the importance of factors like human capital, labour market, and other environmental conditions for the development of PE markets in one way or another.

3.3.6 Entrepreneurial Culture and Deal Opportunities

The amount and quality of investment opportunities are something Groh et al., (2018) regard as the most important allocation criteria that influence the attractiveness of markets. They state that "*The expectation regarding access to viable investments is probably the most important factor for international risk capital allocation decisions. Particularly for the early-stage segment, we expect the number and volume of investments to be related to the innovation capacity and research output in an economy.*" (Groh et al., 2018, p.10). This is linked to the assumption that innovation and research create a larger expected deal flow for investors in a market. The entrepreneurial culture is, as we have mentioned in relation to other criteria, possibly affected by several other factors which create an environment for entrepreneurs and businesses that shape the market.

Blundell-Wignall & Roulet, (2015) point out that the expenditures related to R&D seem to have a positive effect on investments in developed countries**,** and (Adongo, 2011) confirms that the results are similar when focusing on African countries. Kumar & Orleck (2002) establish a link between patents denied and the level of investments. Patents are important tools to create incentives for innovation and research that could also be linked to the security of property rights. On the other hand, Djankov et al., (2002) argue that if the process becomes too complex and time-consuming with a large bureaucracy, it may discourage the entrepreneurial activity. The institutional environment must facilitate a process that does not constrain other activities in such a manner that it depletes the benefits of security and increases the aspect of risk that comes with being innovative.

Chikaonda, (2012) discusses the bi-directional relationship between early-stage investments and innovation. The possibilities of financing for start-ups and Venture Capitalists could also work in a way that it stimulates innovation. We have also seen from the literature that many of these factors work in ways that they are promoting each other and are sometimes dependent on several elements for them to be accomplished. Entrepreneurial activity is closely linked to financing, human and social environment, and several other institutional factors that either create incentives for or discourage the innovation capacity and research output. However, it seems to be a consensus that the entrepreneurial activity and expected deal flow are some of the most important pillars in the allocation criteria framework for investors.

3.3 Summary

The distinct importance of each decision criteria for PE investments, and how each of the components influences the markets in isolation, remains unclear despite a large number of PE studies. There is no doubt that the factors are correlated with each other, and therefore, the importance and relevance of one element are often contingent on other factors. It could be stages of market development or investors preferences that lead to conflicting conclusions based on different samples and periods studied. Nevertheless, most of the possible determinants are comprehensively studied, some more than others, which points us in a direction that some are more relevant than others, given the presence of other factors.
There is evidence showing that the determinants of PE activity differ in developed and developing countries. For instance, the size of the stock market and IPO’s are important for investors in developed markets, while this is not always the case for investors focusing on emerging markets. According to the literature, investor protection and expected deal flow seem to be some of the most important allocation criteria for PE investors in emerging markets.

The aim of most of the research is to explain the differences in the allocation of investments and development of PE markets that is attributed to investors’ allocation decision criteria and external factors. Given the complex nature of the influential power these broad ranges of factors exhibit, the interplay amongst them are vital for the understanding of their relative importance within each market. Groh et al., (2018) cite Black & Gilson, (1998) line of argument calling it a “*chicken and egg*” problem and argue that a country needs to improve several factors in combination to attract more PE capital.

4. Methodology

4.0 Introduction

This chapter focuses on the methodology of the research process and contains a detailed discussion of the techniques used to answer the research questions. The research methodology, recruitment and sampling, data collection, and analysis are presented respectively. Lastly, we will evaluate the quality of the methodological approach by looking at the reliability and validity of the qualitative data and discuss in what way these two requirements were met in the study.

4.1 Aim of Research

The purpose of this study is to investigate the research questions listed below:

1. *What are the drivers that underpin the development of the PE market in Tanzania?*
2. *What are the policy recommendations to improve Tanzania's ability to attract PE investments?*

4.2 Research Methodology

Research is an investigation of finding solutions to scientific and social problems through an objective and systematic search for new and useful information (Rajasekar, Philominathan , & Chinnathambi , 2013). The research format used in investigating a problem statement should be a tool to answer the research questions. Although each research study has its own purpose, the objectives may be generalized into two main categories: exploratory research, which refers to gaining familiarity with a phenomenon or to achieve new insight into it, or descriptive research, which refers to accurately portraying the characteristics of an individual, situation or a group (Kothari , 1990). Exploratory research questions are typically developed when: a) not much is known about a specific phenomenon; b) existing research results suffer from limitations; c) the topic is highly complex; or d) there is not enough theory available to guide the development of a theoretical framework (Sekaran & Bougie, 2016).

This study adopted an exploratory research design as it sought to investigate PE investments in Tanzania. Our motivation for conducting exploratory research derives from the lack of research of the PE industry in Tanzania and the fact that the subject is vastly complex. Tanzania is a country with a short history of PE compared to many other countries, and is still considered to be in an early-stage of its development. Although there exists a large body of research on the determinants of vibrant PE markets, most of them focus on developed countries with a long history of PE activity and more developed markets for alternative investments. To our knowledge, there is limited research that studies what affects and shapes the development of PE in the case of Tanzania. An exploratory approach allows for acquiring new insights and provides a better understanding of the PE market in Tanzania.

4.2.1 Qualitative Data Analysis

The choice of research methodology strongly depends on the nature of the research question. Sekaran & Bougie, (2016) argue that a qualitative method is an appropriate choice when conducting an exploratory study. For an exploratory study with a complex subject and a limited theoretical foundation, such as ours, a qualitative approach was considered to be the most fitting. A qualitative approach allows for greater opportunities of depth and meaning based on PE firms experience and understanding of the factors affecting PE investment in Tanzania. Most of the existing literature on PE markets utilizes a quantitative approach, seeking to quantify and measure the effects of specific factors that are considered to have an impact on the level of PE investments. The limitations apparent with this approach are the use of proxies and the lack of ability to gain a deeper understanding of how the factors affect and shape PE markets. This study aims to explain *what* factors that affect the development of the Tanzanian PE market, and *how* the determining factors contribute to the development.

The PE industry in Tanzania only consists of a few firms and funds, which are mostly foreign, because of its relatively short history. The main characteristics of qualitative research are its appropriateness for small samples, as the outcome may not be measurable and quantifiable opposed to a quantitative approach which is broader in scale and numerically based (Sekaran & Bougie, 2016). Thus, our choice of methodology is suitable for the study's purpose of providing insight into a young and small industry.

4.3 Recruitment and Sampling

This study was conducted in Tanzania using PE firms operating in the country as the main data source. The study's population constitutes PE firms and other stakeholders, such as PE associations in Tanzania. As previously mentioned, the PE industry in Tanzania is relatively small. Therefore, the population size will be accordingly. We were only able to locate four PE firms operating in Dar es Salaam, the largest city in Tanzania, which is an indication of the size of the local PE industry in the country. The sample size extracted from the population consists of four PE firms operating in the country, one DFI and one representative from a PE association for funds in Tanzania. The inclusion of a DFI in our study is based on the important role DFIs have played in the history of financing private enterprises and providing risk capital in Tanzania. The unit of analysis for our study were the organizations, meaning that the informants acted as a representative of the organizations' views and opinions.

There is no need for a numeric representation, as this is a qualitative study and a moderately small sample size is sufficient (Willig, 2013). After interviewing the sixth informant, we reached the conclusion that increasing the sample size would not add any new information to our study. Based on our experience and the data collected from our sample, we found it likely that new themes or ideas would not emerge by conducting additional interviews with participants of the PE industry in Tanzania. Fusch & Ness, (2015) describe this as saturation, which is reached when there is enough information to replicate the study when the ability to obtain additional new information has been attained. Burmeister & Aitken, (2012) argue that data saturation is not about how big the sample size is, but about the depth of the data. A large sample size does not guarantee data saturation, nor does a small sample size; rather it is what constitutes the sample size. Our aim was to get a good quality sample that contributes to the understanding of the local PE market. Participants were recruited on the basis that they operated in Tanzania or were representative of operating firms and chosen purposively.

Key Informants (KIs)	**Category**
KI 1	PE firm
KI 2	PE firm
KI 3	PE firm
KI 4	PE firm
KI 5	DFI

KI 6	PE Association

Table 1: Unit of Analysis

4.4 Data Collection

Data was collected using a two-phased approach, the first one involving secondary data and the other one was the collection of primary data through in-depth expert interviews.

4.4.1 Secondary Data

Phase one included the use of secondary data collection for the analysis of the Tanzanian PE market. The aim of phase one was to use the data to support and complement the data collected under phase two and provide a more reliable research. The study included secondary data in order to gain a better understanding of the PE market in general, as well as a clearer and more detailed analysis of the situation in Tanzania. The use of existing data also contributed to the identification of potential factors affecting the development of the Tanzanian PE market and served as a baseline for the analysis of the primary data. The types of secondary data utilized involved both qualitative and quantitative data in the public domain. The relevant data was mainly collected from various industry and country reports, articles in journals, organisations' websites and books.

4.4.2 Primary Data

The primary data for the study was collected through in-depth interviews with participants from the Tanzanian PE industry. The aim was to gain insight and a better understanding of our research questions through PE experts' views, opinions, and experiences on the subject. Interviewing is a commonly used method of primary data collection as it allows the researcher to collect a wide variety of different data from human respondents (Sekaran & Bougie, 2016). An interview is "*a guided, purposeful conversation between two or more people*" (Sekaran & Bougie, 2016, p. 113)**,** and are among the most recognisable strategies for collecting qualitative data which emerges from a diverse disciplinary perspective resulting in a wide variation among interviewing approaches.

Sekaran & Bougie, (2016) describe both unstructured and structured interviews and discuss the merits and demerits. Unstructured interviews are called so due to the interviewers' lack of planned sequence of questions to be asked of the respondent. The main purpose of an unstructured interview is to explore and investigate several factors in the subject that might be central to the broad problem area and to determine what factors need further in-depth investigation. Structured interviews are those conducted when it is known what data is needed, allowing the content of the interview to be prepared in advance. In this study, primary data was collected using semi-structured interviews, which are characterized with predetermined open-ended questions, with further questions emerging from the dialogue between the interviewer and interviewee (Dicicco-Bloom & Crabtree, 2006). All the informants in our study were subject to the same questions and interview structure. The interview outline consisted of two parts, the first part included questions based on the theoretical framework, while part two were performed with the use of open-ended questions as a way of gaining depth in the interview process. This approach allowed for new themes and issues to emerge during the interviews. The choice to collect primary data through semi-structured individual interviews was on the basis of the complex nature of the PE industry that is subject to different views and opinions from various investors, allowing them to freely express their views in their own terms.

Research Description	**The Aim of the Phase**	**Data Collection Method**	**Sample Technique**	**Sample Size**
Expert interviews	To gain insight into the PE market in Tanzania through PE experts	Face to face or via Skype, semi-structured Interviews	Purposive	Six PE Firms/DFI/Representative of investors

Table 2: Summary of sampling and data collection method

4.5 Data Analysis

Miles & Huberman, (1994) review three general steps in analysing qualitative data: data reduction, data display, and the drawing and verifying of conclusions. Data reduction refers to the process of selecting, coding, and categorizing the data, while data display presents the selected data in an appropriate way. Drawing a conclusion is the final analytical activity in the process, and remains the essence of the analysis, as we provide answers to the research questions by determining what identified themes stands for, by explaining for observed patterns and relationships, or by exposing contrast and comparisons. The interviews provided us with a large amount of information, therefore data reduction was necessary, separating the data into smaller units and categorizing them in order to display only the relevant data. The disassembling of the collected data was done focusing on patterns or links between the theory and literature review, and the study's research questions as well as emerging themes from the interviews.

4.6 Reliability and Validity

"*Reliability is the extent to which a measurement procedure yields the same answer however and whenever it is carried out, and validity is the extent to which it gives the correct answer*" (Kirk, Miller, & Miller, 1986, p.19). To increase the reliability of the study, multiple research methods such as literature review and in depth-interviews were used. Although interviews offer great benefit for qualitative researchers, there is a risk of simplifying and idealizing their interview based on the assumption that interviewees are knowledgeable and moral truth tellers (Alvesson, 2003)**.** Using secondary data such as reports, articles in journals and books to support and assist in the analysis have decreased the risk of simplifying the primary data collected from our interviews. We also considered the nature of our research to be such that it would not provide any obvious benefits for participants to dissimulate or deviate from the truth. In addition, the participants were anonymized to avoid any potential restrictions.

Data produced by interpretive methods such as interviews are described as "*unreliable, impressionistic, and not objective*" (Denzin & Lincoln , 2000, p.16), and regards interviews as nothing more than casual conversations. However, opposed to a regular conversation, the research interview can be characterized by an asymmetry of power where the researcher is in charge of questioning an interviewee. In addition, preparation is necessary to avoid disappointing results. Therefore, to carry out qualitative research, the use of various skills, such as listening, note-taking, and careful and sufficient planning are required (Sandy & Dumay, 2011). In this study, the interview outline was prepared in advance to assure that the same issues were addressed in every interview, but with the freedom to express their views in their terms, allowing an unanticipated conclusion to be discovered.

5. Presentation of findings

The research questions attempt to improve the understanding of the drivers that underpin the development of the Tanzanian PE market, and the policy implications from an investor's point of view. The relative importance of each determinant included in the index created by Groh et al., (2018) for measuring the attractiveness of countries was studied using a qualitative approach. Our findings represent investors' view on the drivers from a Tanzanian investor's perspective and are presented below with a structure similar to the framework of the index.

5.1 Research Question 1

"What are the drivers that underpin the development of the PE market in Tanzania?"

5.1.1 Economic Activity

The question of how economic activity affected the investors' investment decision in Tanzania, included factors such as real GDP growth, exchange rate stability and employment level. There seemed to be an agreement among half of the KIs that economic growth affected their investment decision. KI 1 emphasized that Tanzania is an emerging market with consistent economic growth that still has a lot of untapped potential. This view was confirmed by KI 2 and KI 3, who both stated that it had an effect on their decision to invest in Tanzania. KI 1 also expressed that the Tanzanian market was favourable for investments because of the growing economy combined with a falling inflation rate and a large population. In addition, the PE market was described as a fresh market for investors with many opportunities. Compared to other countries on the continent there are few investors competing, which keep the asset prices lower and give opportunities for higher returns.

KI 5 and KI 6 argued that the effect of economic growth was not a determinant because of the small size of the economy. Further, KI 6 pointed out that the country's economic growth itself was not a determinant because it is important to look at the underlying drivers for the growth. In this case the strong growth did not provide them with additional investment opportunities because the growth was to a large extent driven by other factors than the development of the private sector.

Trade openness was argued to be favourable for investment decisions in Tanzania by KI 1 and KI 6, as they described it as a country with few trade restrictions. However, KI 2 claimed that trade policies were a challenge for specific business sectors, but it did not have an impact on their decision to invest in the country. There were no indications among the KIs that the employment level was an important selection criterion for their allocation of capital.

	GDP Growth	Employment Level	Trade Openness
Key Informant 1	X		X
Key Informant 2	X		
Key Informant 3	X		
Key Informant 4			
Key Informant 5			
Key Informant 6			X

Table 3: Factors Affecting PE Decisions: Economic Activity

5.1.2 Depth of Capital Markets

When discussing the depth of Tanzania's capital market, we refer to the size of the stock market, various exit opportunities, availability of debt and the level of interest rates. The KIs all stated that the size of the stock market was small and not of importance. The stock market in Tanzania was referred to as underdeveloped with few listings and a small market capitalization of the listed companies. The poor and illiquid capital market caused most of the investors to look for an alternative exit opportunity.

KI 1 argued that they might consider an IPO, but because of the small size of the stock market, it is not always the preferred exit strategy. Due to a limited number of PE firms operating in Tanzania, they also look at international firms coming into the country for exit opportunities. KI 2 stated that the most common exit strategy was through a secondary buyout, but that in general, it is challenging to find satisfying exit opportunities. KI 5 expressed that it is difficult to exit, but that there exists a secondary market in Tanzania and that they have not faced any particular challenges. The KIs all agreed that the stock market and the opportunities for IPOs was not favourable, but as long as there existed other modes of exit, the size of the stock market was not a determinant. The KIs expressed that the secondary market was sufficient in Tanzania, and that the existence of alternative exit opportunities was a determinant for PE investors.

KI 1 stated that "w*hen it comes to availability of debt and financing by banking sector Tanzania is behind."* Further, it was claimed that access to debt is one of the biggest problems for entrepreneurs and that this might represent an opportunity for PE firms to enter the market. KI 1 acknowledged the need for affordable long-term capital and indicated that this was an important driver for their investment decision. KI 2 and KI 4 also expressed their concern and stated that "*banks are not reliable and SMEs do not have access to financing*", which makes bank-centred financing very costly for businesses due to high-interest rates and collateral requirements. Moreover, KI 2 emphasized that low availability of debt could affect PE firms negatively as they need to bring in more money if companies struggle to get affordable financing for their working capital elsewhere.

KI 6 shared the concerns over access to debt and said that "f*rom where we sit we find that local debt is shrinking in Tanzania which means that a PE investor has to plough in more capital when businesses do not have access to working capital from local markets.*" The same KI added that "d*eals get more expensive and there are less opportunities to grow investments."* KI 3 pointed out that the availability of debt to some extent depends on the sector and that there are some sectors, such as agriculture that have some special considerations. The same KI expressed that access to financing can be challenging and costly; however, it is possible. Similarly, KI 5 alluded that financing can be a barrier for start-ups, but that this is also since many projects seeking financing lack a viable business plan and qualified management.

All the KIs, except for one, regarded the availability of debt as an important factor to consider in a PE investment decision. KI 2, KI 3 and KI 6 found low availability of debt to have a negative impact on the capital allocation decision, while KI 1 and KI 5 had an opposing view where low availability of debt was considered to be positive for PE investors as this increases the demand for alternative financing.

	Size of Stock Market (IPO)	Other Exit Opportunities	Availability of Debt	Interest Rates
Key Informant 1		X	X	
Key Informant 2		X	X	
Key Informant 3		X	X	
Key Informant 4		X		
Key Informant 5		X	X	
Key Informant 6		X	X	

Table 4: Factors affecting PE Decisions: Depth of Capital Markets

5.1.3 Tax System and Administrative Burdens

The discussion on this subject was mainly focused on how tax regulations and administrative requirements affected the investment decision and the development of the PE market. The KIs shared a similar view that the tax regime was often complex and time-consuming, and not favourable for investors. The different tax rates were not considered to provide any incentives for investments in the private sector.

KI 1 pointed out that the high level of capital gains tax upon exit could be a challenge for investors. Compared to the neighbouring country, Kenya, the tax rate on capital gains are considerably higher, and it was argued that this made Tanzania a less attractive destination for risk capital. KI 2 also highlighted the importance of a stable tax system to facilitate investments as investors often shy away from areas where it is difficult to predict future conditions. Uncertainty and large fluctuations in the tax rates could make it harder to estimate the future value of investments.

The tax regulations were perceived as a barrier by both KI 4 and KI 6 where the former stated that *"the least favourable and most challenging factor affecting our investment decision was the tax regime and investment policies"* and that "*compared to other countries in Sub-Sahara tax rates are still high, and there are many compliance requirements.*" KI 6 agreed that the tax regime is unfavourable and emphasized that the income tax was of particular concern because of the way it is calculated that do not favour investors. KI 5 expressed concerns regarding the tax collection process and stated that businesses with foreign ownership often were subject to stricter enforcement of tax regulations than those owned by locals. They would also experience more harassment from tax officials who would try to take advantage of, and exploit foreign investors on tax matters. This behaviour was perceived as unfair and discouraging for foreign investors.

The level of complexity and time spent on administrative procedures associated with tax were also a major concern that several KIs indicated was equally important. This was considered as challenging and added extra costs to the projects for the investors. KI 2 and KI 4 were those who expressed the greatest concern and argued that the tax system is complicated and there is a lack of information and support. KI 4 added that "y*ou must file a ton of files, which requires much time. This could be costly for us and slow down the investment process*."

After entering the Tanzanian PE market, KI 3 realized that they needed a deeper understanding of the tax regulations and laws in order to comply as it was more complicated than anticipated. Their solution was to hire experts to assist them with tax and administrative related issues. Therefore, despite the challenges with tax regulations, KI 3 argued that the tax system did not affect their decision to invest in Tanzania.

All the KIs, except for KI 3, indicated that the level of tax rates had a negative impact on investment decision. On the next issue concerning administrative burdens, only KI 2 and KI 4 implied that it was an important consideration in the investment decision process.

	Tax rates	Administrative burdens
Key Informant 1	X	
Key Informant 2	X	X
Key Informant 3		
Key Informant 4	X	X
Key Informant 5	X	

Key Informant 6	X	

Table 5: Factors Affecting PE Decisions: The Tax System and Administrative Burdens

5.1.4 Legal System

The KIs highlighted different areas of concern, but there was an agreement that the quality of legal enforcement was challenging in general. The legal system in Tanzania was associated with a high level of uncertainty and insufficient information. The legal enforcement process was described as time-consuming and inconsistent as the legal frameworks are frequently changed.

There seemed to be no significant problems with the protection of property rights; however, KI 3 pointed out that the protection of property rights could be an issue for the investees in particular sectors, but that they have not experienced any challenges that would question further investments.

The main focus with regard to the uncertainty of the quality of legal enforcement was the country's attitude toward international arbitration. Tanzania has implemented laws that ensure that investor-state disputes are resolved locally with limited possibilities to resolve cases with the use of international arbitration bodies. KI 1 stated that "i*t is a disadvantage for foreign investors because the government is involved in most cases and this might cause conflicts of interest*" and "*this will make it more difficult to attract investors because most foreign investors prefer to have their legal claims resolved in another country.*" This sentiment is shared by KI 5 who argued that the uncertainty and the lack of trust in a fair settlement of disputes are discouraging investments. The same KI also indicated that this has been an important factor in explaining the decline in investments, and why the country struggles to attract foreign capital. KI 6 added that the decline in PE investments is attributed to the level of uncertainty for investor protection and that investors need assurance and consistency.

Moreover, KI 2 implied that the quality of legal enforcement might be a reason for investors not to invest and was further described as "*poor, unreliable and time consuming*" and that "*the legal enforcement cannot be trusted and are not favourable for investors.*" According to KI 6 the legal system was experienced as very rigid, and the system of contract enforcement was described as ineffective. KI 3 held similar views and argued that the legal system in Tanzania was the least favourable factor for investors. There is insufficient information, and the laws are changed frequently making it harder to know what laws are applicable and the implications for investments. Further, the time spent on ensuring that everything complies with the local laws and regulations was emphasized. The legal enforcement process can be very time-consuming, which is why KI 3 sought professional assistance to avoid any major legal disputes. The same KI stated that "*we have used many resources to understand the legal system, and this has been one of our biggest costs.*"

There were also some indications that the issue with the quality of legal enforcement was not specific to Tanzania. KI 1 argued that legal enforcement is reliable in general, but that some difficulties in the process can occur, similarly to most other countries on the continent. Protection of property right was not perceived as an important factor in the PE investment decision process. However, the majority of the KIs emphasized the importance of the quality of legal enforcement. While some focus on the problem of impartial courts, others expressed concerns about the quality of the legal system in general. Nonetheless, there seems to be a general agreement that the legal aspect is an important determinant for investment decisions.

	Protection of Property Rights	Quality of Legal Enforcement
Key Informant 1		X
Key Informant 2		X
Key Informant 3		X
Key Informant 4		
Key Informant 5		X
Key Informant 6		X

Table 6: Factors Affecting PE Decisions: The Legal System

5.1.5 Human and Social Environment

The question of how the human and social environment affects the PE investment decision includes the discussion of education and human capital, labour market rigidities and bribery and corruption. The overarching consensus amongst the KIs relating to education and human capital, was that the ability to attract qualified and competent management was of importance to both PE firms and investees. The general view was that finding skilled people with professional qualifications in the workforce and the low level of education was challenging. KI 1 describes Tanzania as a country with a large labour force, however, the level of employment is low, and many fail to gain employment after graduating.

When discussing the advantages and disadvantages of the large labour force and the low education level, it was pointed out that the low employment level could be favourable, but that the low level of skills and qualifications is disadvantageous. The large supply of labour combined with limited job opportunities leads to favourable conditions for the employers as their bargaining power increases. It was expressed that "*the labour is cheap and that there is plenty of people willing to work in Tanzania which is good for PE firms and businesses.*" That said, KI 1 argued that the problem is to find people with the desired professional qualifications. There is great potential with many graduates from the universities, but the problem lies within the education system and the quality of education. The lack of human capital was described as a barrier because it is challenging and time-consuming to find the right people.

According to KI 1, many businesses lack a qualified management team and PE firms need to use more resources in the process of finding and training people. KI 2 agreed with this view and claimed that education and human capital are important factors in PE capital allocation decision. The same KI cited that "*many people are poorly educated which makes it hard to find competent people for businesses and deals. Knowledge and basic skills are lacking, which prevent companies from fast growth. There is a need for more training and follow-up post investment.*" For a foreign entity coming into the country, finding competent people to match their strategy was described as a problem by both KI 5 and KI 6. It was also emphasized that it could be difficult to bring in foreign expertise because of labour and employment regulations.

KI 3 and KI 4 confirmed that education and human capital are important considerations for PE firms. However, they have not been affected in the same way by the low level of education and human capital as described by the other KIs. The former stated that their connections and good network played an important role in overcoming the difficulties of finding competent people. Further, the importance of social skills, integrity, and ethics are highlighted as they stress the need to find trustworthy people. On the other hand, KI 4 expressed that the low level of education and human capital is generally more challenging when PE firms invest in younger entities. According to KI 4, PE firms that focus on later stage financing face fewer difficulties as "*well-established companies generally have a reasonable amount of human capital.*"

The reflections from the KIs regarding labour market rigidities indicated that it was not a determinant. Nevertheless, it was pointed out by KI 1 and KI 2 that labour protection laws could sometimes be experienced as rigorous and problematic. The hiring and firing practice combined with the complex legal system can be challenging.

The overall view on bribery and corruption implied that it was not an important consideration for PE investors. Several of the KIs exclaimed that it usually did not affect the investors in any significant ways and that it is easy to keep a distance from it. KI 1 pointed out that it has been a widespread bribery and corruption culture, but recent anti-corruption policies from the new government have decreased the extent of it.

	Education and Human Capital	Labour Market Rigidities	Bribery and Corruption
Key Informant 1	X		
Key Informant 2	X		
Key Informant 3	X		
Key Informant 4	X		
Key Informant 5	X		
Key Informant 6	X		

Table 7: Factors Affecting PE Decisions: Human and Social Environment

5.1.6 Entrepreneurial Culture and Deal Opportunities

When discussing the importance of entrepreneurial culture and ease of starting a business, the KIs agreed that these are important factors that affect deal opportunities for PE firms. However, the KIs held differing views about the situation in Tanzania and how these factors affected their investment decision. The majority of the KIs expressed that the mindset of entrepreneurs was different in Tanzania with a limited culture for innovation and growing their businesses. KI 1 cited that "*most Tanzanians start businesses for survival and not for success. They just want food on the table, and have limited mindset when it comes to growth*" and further stated that "*there are many businesses, but they lack a willingness to grow, resources and proper structure*", indicating that there are several potential deal opportunities in the country despite the poor entrepreneurial culture. The same KI perceived the level of deal flow to be a factor affecting their investment decision, but argued that the challenge is the investees fear of losing control and their limited ability to have a long-term perspective. The KI illustrated that "*Tanzanians will choose to earn 10 000 shillings with 100 percent control rather than 20 000 shillings with 20 percent control.*" KI 2 shared this point of view and implied that especially smaller businesses are reluctant to give up control and that sometimes it is necessary to make an extra effort to ensure that they are aware of the potential benefits.

KI 5 described the entrepreneurial culture as poor compared to other countries in East Africa and emphasized that this leads to fewer deal opportunities for PE investors in Tanzania. Investors are more likely to deploy their capital where the culture for starting and growing businesses are more aligned with an investor perspective and consider Tanzania as a less attractive destination for their capital. It was indicated that the entrepreneurial culture and the limited deal opportunities affected their investment decision negatively.

The culture and low level of innovation were also considered as challenging for PE investments by KI 3, who expressed that the element of innovation was important in their selection process. Although it sometimes required much time and recourses to locate deal opportunities; KI 3 focused on the fact that there is a demand for PE firms as there exists a number of potential deal opportunities. KI 6 had a more positive view on deal flow and argued that it is reflected in a large number of start-ups and investment opportunities. Similar to KI 1, both of these KIs considered deal opportunities to be a determinant.

The question concerning the ease of starting a business revealed differing views among the KIs. The process of registering and starting a business was described as "*easy, straightforward, and efficient*" by KI 3, in contrast to KI 1 who argued that the process was time-consuming and complicated. The latter also emphasized that the ease of starting a business might vary depending on the type of business and the sector. KI 2 agreed that the process was complicated and unfavourable as it is difficult to register and a high level of bureaucracy. However, they were aware of the challenges before investing and claimed that it is not a factor that they consider to be important when evaluating the attractiveness of the market.

	Entrepreneurial Culture	Deal Opportunities	Ease of Starting a Business
Key Informant 1		X	
Key Informant 2			
Key Informant 3		X	
Key Informant 4			
Key Informant 5	X	X	
Key Informant 6		X	

Table 8: Factors Affecting PE Decisions: Entrepreneurial Culture and Deal Opportunities

5.1.7 Emergent Factors

The socio-economic factors derived from the theoretical background and literature review were the foundation for the semi-structured interviews which utilized a structure similar to what Groh et al., (2018) proposed for their index of country attractiveness. The use of open questions and the nature of the interviews allowed for other factors to emerge based on additional information provided by the KIs. In the discussion of what factors were important for understanding the investment decisions and the development of the PE market in Tanzania, several factors not covered separately in the literature review, were brought to attention by the KIs and are listed below:

- Political Stability
- Country Perception
- Geographic Location and Climate

The importance of political stability was highlighted by the majority of KIs and considered as a determinant for the level of attractiveness for PE investors in Tanzania. The general view was that the history of a stable political climate made Tanzania more attractive for investors. Further, it was pointed out that Tanzania was located in an area surrounded by many countries with a history of political instability, but that Tanzania was recognised for its peaceful environment, and absence of conflicts and radical changes. KI 3 stated that "*political stability made Tanzania a more attractive destination for risk capital compared to other less developed countries.*" KI 1 commented that "*political stability is highly important for investors to be able to commit to a country by investing*" and that "*Tanzania have never had wars, strikes or any major events that shake the economy.*"

In contrast to the positive views on the favourable history of a stable political climate, the KIs indicated that there was a growing concern about recent political trends. This view was in particular mentioned in relation to the election of the new government and the political changes it has caused. KI 2 mentioned that "*interference in the market, freedom of speech, tax, human rights and safety are issues that might discourage investments.*" Moreover, KI 6 attributed political risk as the number one factor for the stagnated PE activity and argued that the level of PE investments has slowed down because of changes in the regulatory scope and political spotlight, which have made investors less comfortable, at least until they stabilize. Several KIs also expressed that consistency in policies and the conditions for investors are important and facilitates a better investment climate. The uncertainty caused by the recent changes, and the interconnection of political stability and the factors affecting investments has made investors more reluctant.

Investors' perception of a country was also a theme that emerged from the interviews as it was implied that it affected investment decisions. Recent events and headlines have altered many foreign investors' perceptions of Tanzania and its investment climate, making them adopt a more negative attitude towards the country. According to KI 6, the new political situation has increased the perceived risk of the market, not only for PE investments but for the entire private sector. The same KI expressed that the recent political situation has caught much attention and provided many investors with a perception of an unfavourable investment climate. However, it was claimed that investors have a wrong perception of the conditions and that these do not have a direct effect on investment. KI 1 shared this point of view and claimed that "*the perception that Tanzania is not a good country to invest in, must be a part of the explanation to the recent decline in investments.*" It seemed to be a consensus among the KIs that foreign investors' perception of a country affects their decision to enter the PE market and allocate capital.

A country's geographic location and climate were viewed as possible factors for a country allocation decision that could contribute to the explanation of the level of PE investments. For the case of Tanzania, it was argued that both the location and climate were factors that had a positive impact on the country's attractiveness. KI 6 emphasized that Tanzania is a corridor that links many countries in East Africa. The long coastline and easy access to other markets increase trade opportunities and might increase deal opportunities for investors. Several KIs highlighted that Tanzania also benefits from a large agriculture sector and a favourable climate that makes the country attractive to investors. KI 4 suggested that "*the tropical climate and large areas of land suitable for agriculture make Tanzania more attractive in contrast to other countries.*"

	Political Stability	Country Perception	Geographic Location	Climate
Key Informant 1	X	X		
Key Informant 2	X	X		X
Key Informant 3	X			
Key Informant 4	X			X
Key Informant 5		X		
Key Informant 6	X	X	X	

Table 9: Factors affecting PE decisions: Emergent Factors

5.2 Research question 2

"What are the policy recommendations to improve Tanzania's ability to attract PE investments?"

This section highlights specific concerns for the development of PE activity in Tanzania and the policy implications from an investor's point of view. It differs from the previous discussion about the determinants for investment decisions in a way that it focuses on the negative aspects affecting the PE market that could be improved to facilitate more investments. The semi-structured interviews were constructed in a way that let the interviewee speak more freely and highlight areas of concern that affect their investments.

From the discussion, it emanated five key topics:

- Legal system
- Tax System
- Administrative Burdens
- Education System
- Infrastructure

5.2.1 Legal System

The main concerns related to the legal system were the lack of information and international arbitration. KI 3 and KI 4 pointed out the deficiencies in the Tanzanian legal system, where they emphasized the complexity and the amount of time spent trying to understand the system. As a result, investors end up spending time and resources on issues that could have been used in more productive ways. The KIs implied that there is a need for more and better information on what laws are applicable and the legal process. In addition, it was argued that the legal processes need to be more time efficient, as this would ease the overall investment process and increase the profitability of the investments. Better access to information and more efficient processes would reduce uncertainties for investors and increase the willingness to invest.

The laws on international arbitration were considered as highly unfavourable for investors. The degree of investor protection was questioned in specific sectors as these laws have restricted the investors' possibility to settle disputes internationally. KI 5 emphasized that for larger investments, it would not be acceptable for disputes to be resolved locally. Both KI 1 and KI 5 indicated that this reduces the attractiveness of the country from an investor's point of view, and agreed that investors should be able to resolve disputes with recourse to international arbitration. It was implied that this policy was a part of a negative attitude from the authorities towards investors which is causing PE activity to stagnate. Therefore, it was expressed that the option of international arbitration is necessary to increase the level of investments.

5.2.2 Tax System

The KIs stated that the tax rates and the system of tax collection provided investors with few incentives, and that the conditions were not contributing to a favourable investment climate. Compared to other countries in sub-Sahara, the tax rates were high and considered to be more unfavourable. The tax collection system was also perceived as discouraging to investors due to inconsistency and discrimination against foreign investors. KI 5 indicated that the tax system was unpredictable, particularly for foreign businesses, making it hard to estimate the frequency and the amount of tax that must be paid. There was a general agreement that the tax rates should be lowered and constructed in a way that give investors more incentives to enter the PE market in Tanzania. It was suggested that a lower capital gains tax rate and a system similar to the neighbouring country Kenya would be more conducive to investments. The KIs also highlighted the importance of a predictable and reliable tax system that would make it easier for investors to predict future costs and gain trust in a fair system.

5.2.3 Administrative Burdens

The level of bureaucracy and ease of starting a business were pointed out in the discussion of administrative burdens as areas with a need for improvement. It was expressed that there was a lot of unnecessary protocols and that the processing time can be slow in many cases. Time and resources spent on tax compliance, applications, and registrations and licensing were considered to be a burden for investors and businesses, as this affect the profitability of investments and makes the process of starting a new business more challenging. In order to promote more start-ups and reduce the costs and uncertainties for investors, it was suggested that the policymakers should focus more attention to these areas. KI 1 and KI 2 argued that the process and requirements of starting a new business need to be less time-consuming and complicated with better access to information for entrepreneurs. The same was stressed for the process after obtaining a business licence, as the KIs argued that the areas of tax compliance, applications and administrative procedures in general need to be more efficient.

5.2.4 Education System

The low level of human capital and the lack of qualified people was blamed on a weak and underdeveloped education system that is not sufficient in providing people with the necessary skills and competence. PE firms struggle to find qualified people and management teams, and indicate that this is one of the factors that explain the low level of PE activity in the country.

KI 6 cited that "*Tanzania has a closed education system*" and described it as "*rigid and not up to date with the market needs in terms of competence.*" In addition, it was expressed a concern with the limited use of English in their education system compared to other countries in the region, and that this might have a negative effect on communication skills. There was a general consensus among the KIs that the education system needs to be improved in order to increase the level of human capital. It was implied that policymakers should increase their focus on higher education and that the education system needs to keep in touch with the market. KI 3 emphasized that there is also a need for improving the quality of the education as "*people graduate just to graduate, and not actually learn.*"

5.2.5 Infrastructure

Lastly, in the discussion of the necessary efforts to facilitate more investments, improvement of the infrastructure was considered to be of great importance to the business environment which in turn could increase the country's attractiveness for PE investors. The country's large size and location strengthen the need for better infrastructure in the form of transport systems, power supply and telecommunication system. The country's infrastructure was described as "*underdeveloped and challenging*" by KI 1. This sentiment was shared by KI 2, who added that "*infrastructure is bad and makes logistics costlier, and makes firms less profitable.*" It was expressed a need for the government to focus on improving the infrastructure, whereas the transport systems and information systems were highlighted.

5.2.6 Summary

Focusing on the drivers that underpin the development of the PE market in Tanzania, the study findings show that several factors reviewed in the existing literature were also found to have an effect on the PE activity in the case of Tanzania. Furthermore, the findings revealed determinants for the Tanzanian PE market that were not covered separately in the literature review. The majority of the KIs had similar views, confirming that GDP growth, other exit opportunities, tax rates, the legal system, and education and human capital are essential and key factors in the success of PE in Tanzania. The importance of political stability and country perception were also highlighted by several and represents factors that emerged during the discussion. Figure 5 illustrates the mentioned key factors, in addition to other factors that were considered to have an effect by some respondents, but did not represent the general consensus among the KIs.

The last section of this chapter highlighted areas of concern for the development of the PE market in Tanzania from an investor's perspective along with the policy implications. From the discussion, there were five key areas in need of improvement, that were brought to attention; legal system, tax system, administrative burdens, education system, and infrastructure. It was suggested that an increased effort from the policymakers to improve these areas could increase the country's attractiveness for PE investors.

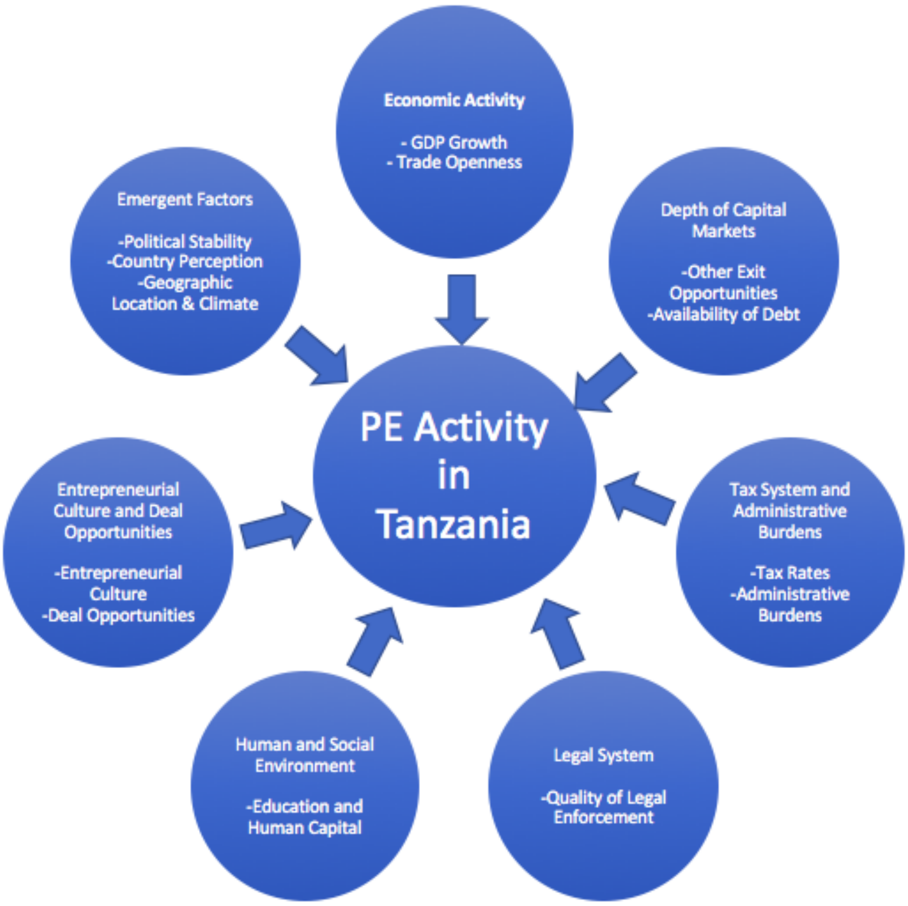

Figure 5: Factors Affecting PE Activity in Tanzania

6. Discussion of findings

6.1 Introduction

A discussion of the results presented in chapter five will be provided as an analysis in light of the existing literature introduced in chapter three, and the background presented in chapter two. The framework presented by Groh et al., (2018) in their index of country attractiveness served as a base for the interviews, and as the underlying theory for answering the primary research question. The discussion of findings will follow the same structure as the previous chapter.

6.2 Research Question 1:

"What are the drivers that underpin the development of the PE market in Tanzania?"

6.2.1 Economic Activity

Groh, (2009) argues that a country's economy affects the national PE market, and that expectations of economic growth require investment and provides a rationale for investors to enter a market. Gompers & Lerner, (1997) shared this view and further expressed that if the economy is experiencing rapid growth, then there may be more opportunities for entrepreneurs to start new businesses, and therefore more investment opportunities for PE investors.

Tanzania continues to experience high economic growth (World Bank , 2017); however, the findings from the interviews revealed that only half of the KIs considered economic growth to have an effect on their investment decision. These described the rapid growth as favourable for investments. The remaining KIs held differing views and argued that the effect of economic growth was not a determinant because of the small size of the economy. It was implied that despite the economy's high growth rate it did not provide them with additional investment opportunities. This sentiment is in line with the studies by both Jeng & Wells, (2000) and Felix et al., (2007) where GDP growth was not found to have any significant effect on the level of PE investments.

The different views on the importance of economic growth as a selection criterion for investors are reflected in the contradictory results from the studies presented in the literature review. Emerging markets are often associated with higher growth rates, but existing literature provides an unclear answer to the effects this have on the level of PE activity. Fast growing economies could represent opportunities for high returns for investors with higher risk willingness or be included to diversify their risk capital investment portfolio. However, the high risk associated with emerging markets could also discourage more risk-averse investors.

While some argue that the assumption of high growth rates is what attracts investors to less developed markets, our findings suggest that the importance of economic growth also depends on the size of the economy. Although, Tanzania is a country with high economic growth the findings indicate that high growth in small economies does not necessarily contribute to a substantial increase in deal opportunities for investors. Moreover, it was implied that it is important to consider the quality of the growth and if the growth facilitates a better investment climate and in fact, creates more deal opportunities.

The country's trade openness was perceived as a factor affecting investment decisions by KI 1 and KI 6, who emphasized that it was favourable for them as there exist few trade restrictions. The majority of the KIs however, did not consider trade openness to be important in their investment decision. This view concurs with the findings of Oni, (2017) that concludes that trade openness does not have a significant effect on the level of PE investment.

The findings implied that the level of employment had no direct effect on investment decisions, confirming the findings of Oni, (2017) who showed similar results. Groh et al., (2018) suggest that the employment level is a proxy for prosperity and might be reflected in other factors that in turn could have an effect on PE activity.

This study revealed evidence that supports the findings of Groh, (2009) who argued that economic activity affects PE investment decisions and that emerging markets attract PE investors due to the expected economic growth rates. Our results suggest that economic growth is an important factor for investors in Tanzania; however, it was implied that the size of the economy, as well as the quality of the growth, could have an effect on the importance of economic growth.

There were also some indications that trade openness could affect investment decisions. Although the majority of the KI did not express that they considered trade openness to be important in their investment decision, it might be the case that investors have a broader perspective, and do not consider every subset in isolation when evaluating the attractiveness of a country. Therefore, it is possible that other indicators of economic activity are reflected in the size and the growth of the economy as allocation criteria in their investment decision.

6.2.2 Depth of Capital Markets

Capital markets play an important role in economic development as it accumulates domestic savings and mobilize foreign capital for long term investments. Nonetheless, capital markets are often underdeveloped or even non-existing in emerging markets (Bruno & Drexler, 2016). Black & Gilson, (1998) highlight the need for an exit strategy by the fund from its investment, and further argue that a well-developed stock market allows for IPO exits, and that it is a determinant in a vibrant PE market.

Gompers & Lerner, (2001) argue that a public listing of the invested company is the ultimate and most successful form of exit. However, our findings showed that the size of the stock market and possibilities of IPO exits were not determinants for PE investors in Tanzania. The stock market was described as underdeveloped with few listings, but the KIs all agreed that as long as there existed alternative exit opportunities, it did not affect their investment decision. The existence of other modes of exit was considered as a determinant for investors in Tanzania, emphasizing that secondary markets for buyouts are vital, especially in the absence of a liquid stock market.

Further, our findings showed that the majority of the KIs considered the availability of debt to be a determinant for investment decisions in Tanzania. However, the results seemed to be contradicting. Some of the KIs had a similar view as Wächter, (2012) who argued that the easier it is for start-ups to get financing, the more investment opportunities there would be for PE firms, implying that low availability of debt has a negative impact on the level of PE activity. In addition, it was pointed out that it could be a challenge for PE firms when businesses do not have access to affordable financing from financial institutions, and PE investors might also have to cover other financing needs such as working capital.

Other KIs held an opposing view and considered low availability of debt to have a positive effect on investment opportunities, as it increases the demand for alternative financing. This view is in line with Olomi & Mori, (2015) who indicated that inaccessibility of debt might increase the demand for PE investments. Young and small businesses in Tanzania have an unmet need for financing, which provides opportunities for PE investors to meet this demand with its provision of alternative capital and fill the gap.

This study found the presence of other exit opportunities and the availability of debt to be important factors affecting PE investment decisions in Tanzania. The investors emphasized the importance of a secondary market that provides opportunities for successful exits as an allocation criterion. Moreover, the findings revealed opposing views on the effect of the availability of debt, as it was expressed that low availability of debt could have both a negative and a positive effect on investment decisions in Tanzania.

6.2.3 Tax System and Administrative Burdens

Groh et al., (2018) argue that there are many considerations with regard to taxation that might shape the PE market directly or indirectly. Although it is reasonable to believe that low tax rates and a favourable tax regime attract investments, the link between tax and the level of PE investment is not straightforward. Countries that attract the most PE capital are not necessarily those with the most favourable tax systems, and many countries that struggle to attract investments have a tax system that provides more incentives for investors.

Similar to the studies of Gompers & Lerner, (1997) and Adongo, (2011), our findings support the reasonable assumptions that higher tax rates have a negative effect on the level of PE investments. The majority of KIs, 5 in total, indicated that the level of tax rates and the tax regime were important considerations for their investment decisions. It was expressed concerns about the level of tax rates, and the tax collection process that was described as unfavourable, especially for foreign investors. The KIs implied that this could be a barrier for investors, and a factor explaining the low level of PE activity in Tanzania.

The administrative burdens associated with the tax system were also perceived as important considerations by some, as it was described as complex, inconsistent and time-consuming. This led to increased costs related to administrative procedures and ineffective use of resources that could have been used for value creation. However, the majority of the KIs did not share this concern but focused on the level of tax rates and tax collection in their investment decision.

Although the KIs expressed concerns about different aspects of the tax system such as the level of tax rates, policy inconsistency, and administrative burdens, it was implied that these elements of concern were related to each other and reflected the tax system in general. All the KIs, with the exception of one, perceived the tax system as an important factor to consider in their investment decision, and agreed that it could affect the attractiveness of Tanzania for PE investors.

6.2.4 Legal System

Groh et al., (2018) argue that legal structures and the protection of property rights have a significant effect on the attractiveness of PE markets. This view concurs with La Porta et al., (1997) who argue that a good legal system protects potential investors against the expropriation of their assets and increase their willingness to invest in securities, thus extending the scope of the capital market. Further, La Porta et al., (2002) show that low protection of property rights and minority shareholder rights might lead to a higher cost of capital and lower firm valuation. Further, Kumar & Orleck (2002) find that cost of capital and the legal system have an effect on PE allocation.

The KIs expressed that investor protection in Tanzania was associated with uncertainty and insufficient information, and described the legal enforcement process as time-consuming and inconsistent. The main concern regarding investor protection was the uncertainty related to the independence of the judiciary and a fair settlement of disputes. The implementation of the new laws that restrict the use of international arbitration affects specific sectors, especially those dealing with natural resources, due to a large degree of government interaction. Our findings indicate that these new laws lead to lack of trust in a fair settlement and that it is discouraging for investments in Tanzania, as it was implied that the government might gain an advantage when resolving disputes in Tanzanian courts.

Groh et al., (2018) argue that doing business becomes more costly when there is a lack of legal protection and enforcement possibilities. This sentiment is especially relevant for PE because of the long-term relationships with institutional investors, and as the source of investment can be distant and different from the host countries. The legal system in Tanzania was characterized as complex and time-consuming, and it was stated that PE investors need to use additional resources to understand and deal with an inefficient system. Further, Groh et al., (2018) emphasize that investors need to be confident that their claims are well protected in order to allocate capital. This view was supported by our findings as it was implied that the poor quality of the legal enforcement could be a reason for the low level of PE investments in the country.

In the discussion of the importance of the legal system, the majority of the KIs emphasized the importance of the quality of legal enforcement. Some had specific concerns about the investor protection, while other focused on the quality of the legal enforcement in general. Although the investors focused on different aspects of the legal system, the general sentiment supports the literature that highlights the importance of the quality of the legal system in attracting PE investments.

6.2.5 Human and Social Environment

Studies such as Precup, (2015) and Black & Gilson, (1998) show that a country's human and social environment are relevant in explaining the development of PE activity. Groh et al., (2009) observe that limited partners rely on the skills and quality of the general partners, and that PE firms base their investment decision on the skills and quality of the entrepreneurial management. Our findings support these sentiments and show that the human and social environment have an effect on PE investments decisions. However, the focus of the investors seemed to be on the supply of human capital, and not on labour market rigidities or bribery and corruption.

All the KIs expressed a similar view on the importance of finding businesses with competent and skilled management with the ability to grow the business. The general view was that PE firms had difficulties finding professional people with the right qualifications in Tanzania. The poor education system was pointed out as a reason to why this was considered as a challenge for the investors. The findings indicated that the lack of human capital might affect investments in a way that they need to use more resources for training and follow up. Schertler, (2003) supports this view and shows that higher levels of human capital are associated with increased early-stage investment activity. The findings indicate that because this type of investments involves monitoring and supporting of the enterprises, the costs increase and make investors more selective when choosing businesses to invest in.

Contrary to the study by Groh et al., (2008) that find the fear of bribery and corruption to be of significant importance, our findings show that this was not an important consideration for PE investors in Tanzania. It was pointed out that Tanzania has widespread bribery and corruption culture, but that it did not affect their investment decision as it was possible for PE firms to keep a distance from it.

While Jeng & Wells, (2000) find labour market rigidities to have a negative effect on early-stage investments, the results from our study suggest that this does not affect the investment decision for PE firms in Tanzania. The rigidity in the labour market with respect to labour protection laws was described as challenging in some cases, but it was not a determining factor for PE investors.

There was a general consensus among the KIs that the level of education and human capital was the most important factor for PE investors in the discussion of the human and social environment. Although all the aspects of the human and social environment covered were described as unfavourable to some extent, it was only the low level of human capital that seemed to be a determinant for PE investors in Tanzania.

6.2.6 Entrepreneurial Culture and Deal Opportunities

Groh et al., (2018) highlight the importance of the level of investment opportunities and consider it to be the most important factor for PE investors' allocation decisions. In their earlier study of PE in emerging markets, they argue that expected growth and entrepreneurial opportunities are what attracts investors. Economic and entrepreneurial activity is what creates deal opportunities, and without any deal flow, there would not be a reason for investors to consider allocating capital to a country (Groh, 2009).

The findings implied that Tanzania is a country with a poor culture of innovation and growing businesses. The entrepreneurial mindset was described as limited as most of the business owners lack a willingness to grow. All the KIs expressed concerns about the entrepreneurial culture, yet there was only one that perceived it as a determinant for their investment decision. The entrepreneurial culture affected their decision negatively and it was considered to be a factor that explains the low level of PE investments in the country.

In the discussion on how the expected number of deal opportunities affected the PE investors' willingness to invest in Tanzania, there were differing opinions. The majority of the KIs indicated that the number of deal opportunities in the country had an effect on their investment decision. Half of the KIs had a positive view of the deal flow in Tanzania and implied that this is one of the factors that attract investors to the country. This view is in line with Groh, (2009) who argues that entrepreneurial opportunities are what attract PE investors to emerging markets. However, one of the KIs expressed concerns about the number of deal opportunities, indicating that this have a negative effect on investment decisions for PE investors in Tanzania.

The KIs held opposing views of how easy it is to start a business in Tanzania. On the one hand, it was expressed that registering and starting a business were relatively easy and straightforward. On the other hand, it was stated that the process of starting a business is complicated and unfavourable for start-ups as there is a high level of bureaucracy. Djankov et al., (2002) argue that if the process of starting businesses is complex and time-consuming as a consequence of a large bureaucracy, it could affect the entrepreneurial activity and lead to less potential deal opportunities for PE investors. This might also be the case for Tanzania, whereas the ease of starting a business combined with the entrepreneurial culture affects the number of start-ups negatively. The ease of starting a business in isolation was not considered as an important determinant for PE investors in Tanzania; however, it is reasonable to believe that it affects deal opportunities which in turn was considered to affect the investment decision.

The findings show that the majority of the KIs consider the deal opportunities to be a determinant in their investment decision. As expressed by Groh, (2009) the existence of deal opportunities is vital for attracting investments, and investors are usually attracted by a large number of investment opportunities, which characterizes emerging markets. Our results indicate that investors in the Tanzanian PE market have differing views on the access to viable investment opportunities, but the majority agreed that it was an important consideration. The majority did not express any specific concerns about the ease of starting a business or entrepreneurial culture with regards to the investment decisions, but is likely that this could have an effect on the number of deal opportunities.

6.2.7 Emergent Factors

The inclusion of the factors that emerged during the interviews was important in order to obtain a deeper understanding of the development of Tanzania's PE market. These factors were not covered in depth nor a part of the framework in the theory and literature review, but the investors' focus on these themes are reasonable in the light of Tanzania's characteristics and political economy.

•Political Stability
•Country Perception
•Geographic Location and Climate

Compared to many of its neighbouring countries, Tanzania are known for its history of political stability. The majority of the KIs highlighted the importance of a stable political climate for investors and stated that it makes Tanzania a more attractive country for risk capital allocation compared to other developing countries. The findings indicated that the absence of conflicts and radical changes in the political economy benefits PE investors by reducing uncertainty. Although the country continues to benefit from a stable political economy, the KIs raised a concern about the recent political situation. According to the KIs, the changes after the last election in 2015 marked the start of a period with increased uncertainty and a more negative outlook from investors. The changes in policies and laws that were implemented by the new government have affected the investment climate, and were described as unfavourable and unpredictable for investors. The KIs lamented the need for policy consistency in areas that affect the business environment. Further, it was discussed that the slowdown in PE investments in Tanzania could be attributed to the increased uncertainty among investors, which has made them more cautious. While the economy continues to grow rapidly, private investments have not followed the same path, and as the KIs implied; this might partly be due to the increased uncertainty caused by the changes implemented by the new government.

Following the previous discussion of political stability, it was also argued that the investors' perception of the country and its investment climate have changed. There has been a series of events and headlines, such as human right violations, restriction on political activity and laws to control the media that have questioned the country's political stability, and have made investors more negative toward the country. It was implied that this has increased the investors' risk perception of the investment climate in Tanzania and that investors now perceive Tanzania as a more unstable country. However, the perceptions do not always reflect the actual conditions for investors in Tanzania, and it was stated that the negative view was sometimes exaggerated. The findings indicated that the perceptions of the country have affected investment decisions and could contribute to the explanation of the recent decline in PE investments.

Geographic location and climate were also factors that emerged in the discussion of what affect the development of the Tanzanian PE market. The KIs argued that the country benefits from the favourable geographical location, as it links many countries in East Africa and has a long coastline, which increases trade opportunities and provides more business opportunities for PE investors. The climate was also perceived as favourable, with regard to the large agriculture sector and tourism. The findings imply that these conditions increase the number of deal opportunities and make Tanzania more attractive to PE investors.

6.3 Research Question 2

"What are the policy recommendations to improve Tanzania's ability to attract PE investments?"

From the discussion, it emanated five key topics:

- Legal system
- Tax System
- Administrative Burdens
- Education System
- Infrastructure

6.3.1 Legal System

The main concerns regarding the legal system were considered to be the complexity and the lack of general information, in addition to the laws restricting international arbitration. It was implied that investors have to use additional resources in order to understand the legal system and the laws that might affect their investments. Investors would benefit from a legal system with easy access to information and more efficient processes, as they could use their resources in a more productive way. The recent legislative amendments that include the restriction of international arbitration have also caused concerns for foreign investors. The new laws on international arbitration will discourage foreign investment, especially investment in sectors dealing with natural resources. Foreign investors lack trust in a fair settlement, and it was implied that this was a part of a trend where the government have adopted a more negative attitude towards the private sector in Tanzania. The KIs indicated that the option of settling disputes internationally is necessary in order to increase the level of PE investments in the country.

6.3.2 Tax System

The tax system was in general described as unfavourable in Tanzania as it provides few incentives for investors. The new government's focus on raising revenues has led to more aggressive tax collection systems, which was considered as arbitrary and harassing by many investors. The findings implied that the tax system was unpredictable because of inconsistent policy implementation and biased targeting. These new actions from the government to improve tax discipline have increased the uncertainty among investors and led to concerns about unexpected tax increases and erratic regulatory changes. The tax rates were also described as unfavourable and made Tanzania less attractive compared to other countries in Sub-Sahara. The implications from the findings were that the tax rates need to be lowered and that a tax system similar to other neighbouring countries would provide more incentives for foreign investors. The government should focus on making the tax system more predictable and reliable so that investors are able to anticipate future costs and build trust in a fair tax system.

6.3.3 Administrative Burdens

The time and resources spent on administrative procedures were highlighted as a concern for investors in Tanzania. The process related to tax compliance, applications, and registrations and licensing were described as time-consuming and perceived as areas that needed improvement. It was argued that the administrative burdens affected the profitability of investments and discouraged new start-ups. The findings implied that policymakers should reduce the number of protocols, which were described as unnecessary, and make the administrative procedures more efficient to facilitate increased entrepreneurial activity and reduce the costs and uncertainties. There is also a need for better access to information for entrepreneurs and investors, to help them understand the processes and requirements.

6.3.4 Education System

PE firms in Tanzania have difficulties finding qualified people and businesses with a competent management team. The education system was described as underdeveloped and rigid, and pointed out as the main reason for the lack of human capital. The system is not able to educate enough people with the competence and skills needed in the job market. The implications from the findings were that the government should prioritize improving the quality of higher education and that there should be a stronger link between the education system and the job market. The problem is not the number of graduates in the country, but the quality of their education and the fact that it fails to provide people with the skills expected in the job market.

6.3.5 Infrastructure

Tanzania's infrastructure was described as poor and underdeveloped, which is a challenge for many businesses in the country. The transport systems, power supplies and information systems are areas that need improvement to unlock the country's growth potential and facilitate more investments in the private sector. The KIs expressed that the country's large size and location increase the need for better infrastructure. The findings indicated that to improve the overall business environment, policymakers need to prioritize investing more in infrastructure and particularly in areas such as road networks and telecommunication systems.

7. Conclusion

7.1 Introduction

The global PE industry has experienced a continuing increase in capital raised and invested in the last decade. Moreover, we have witnessed an even stronger growth for the PE industry in the East African region. Despite the growth in capital invested in the region, Tanzania has not been following the same trends and struggle to attract PE investments. Tanzania is a country with high GDP growth and great potential; therefore, it is interesting to study the underlying reasons for the low PE activity. This research aimed to provide an understanding of the factors affecting the development of the PE market in Tanzania. Our primary research question sought to explain the factors and the way they affect PE allocation decisions. The secondary objective of this study was to highlight the policy implications specific to Tanzania that could make the country more attractive for PE investments.

7.2 Principal Findings

The underlying theoretical framework of this research is based on the socioeconomic factors included in the PE and VC Country Attractiveness Index by Groh et al., (2018). Our study utilizes a qualitative approach that allows for greater opportunities of depth and meaning based on PE firms experience and understanding of the factors affecting PE investment in Tanzania.

Economic activity was considered to be an important factor that affects PE investment decisions. Our findings support the assertion of Groh, (2009) who argues that economic activity is an important selection criterion and that PE investors are attracted by the expected growth rates in emerging markets. However, our finding also revealed that the size of the economy and quality of the growth have an impact on the importance of economic growth. From our findings, it is reasonable to assume that other indicators of economic activity such as employment level and trade openness are reflected in the growth and size of the economy and not considered separately as allocation criteria for PE investors.

The stock market in Tanzania is considered to be underdeveloped with few listings, but the implications from our study are that as long as there exist alternative exit opportunities, the size of the IPO market does not affect PE investment decisions. The presence of alternative modes of exit was considered as a determinant for PE allocation decision, and a liquid secondary market is vital, especially in the absence of a well-developed stock market. Furthermore, the findings showed that the availability of debt is a determinant, but it revealed opposing views as the availability of debt could have both a negative and a positive effect on PE activity.

Consistent with the findings of Gompers & Lerner, (1997), which show that capital gains tax rates influence PE activity, our findings indicate that the level of tax rates was an important consideration for PE investment decisions. Higher tax rates seem to have a negative effect on PE activity, and an unfavourable tax system with inconsistent policy implementation and high administrative burdens might discourage PE investors.

Groh, (2009) highlights the legal system as one of the dominant criteria for PE investors focusing on emerging markets. Similarly, we observe that investors consider the legal system in their investment decision when allocating risk capital. Judicial independence and the quality of the legal system, in general, are important to secure investor protection, as it could become costly to invest in a country without proper legal protection and enforcement possibilities.

When considering all the aspects of the human and social environment, our findings show that only the level of human capital seemed to be a determinant for PE investors. Low levels of education and human capital among potential investees can be challenging for PE firms, as they might struggle to find businesses with competent management teams. Contrary to the expectations and findings of Groh et al., (2008) we do not find bribery and corruption to have an effect on PE allocation decisions.

In accordance with Groh, (2009), who argues that entrepreneurial activity and deal opportunities are key drivers for the development of PE markets, our findings show that deal opportunities have an effect on PE investment decisions. PE investors seem to assess the attractiveness of a country based on expected investment opportunities.

Our research suggests that in addition to the factors included in the theoretical framework, there exist some other factors that could contribute to explaining the development of the Tanzanian PE market. There is a growing concern about the recent political situation in Tanzania that increases uncertainty among investors and make them more reluctant to invest, which indicates that political stability affects the level of PE activity in a country. The investors' perception of the country and its investment climate have changed following a series of recent events and headlines. Although the effects on the business environment are most likely exaggerated, it has made investors more cautious, indicating that investors' perception of a country can have an effect on investment decisions.

This study also highlights different aspects that are perceived as barriers for PE activity in Tanzania, and the implications for the policymakers to facilitate more PE investment. The legal system should be improved by providing better access to information, and making processes more efficient, in order to reduce uncertainties for investors and increase willingness to invest in the country. In addition, the option of international arbitration is necessary to secure investor protection. Tax rates need to be lowered, and the government should focus on making the tax system more predictable and reliable so that investors can anticipate future costs and build trust in a fair tax system. The findings implied that policymakers should reduce the number of protocols and make the administrative procedures more efficient, in order to reduce administrative burdens for investors and start-ups. The government should prioritize improving the quality of higher education, and there should be a stronger link between the education system and the job market. Lastly, Tanzania's infrastructure was described as poor and underdeveloped, and it was indicated that policymakers need to prioritize investing in areas such as road networks, power supply, and information systems to improve the overall business environment.

The most obvious findings to emerge from this study is that tax rates, availability of debt, exit opportunities, quality of legal enforcement, education and human capital, deal opportunities, political stability, and investor's perception of a country are the most important factors that contribute to explaining the development of the Tanzanian PE market. As it is emphasized in the existing literature, our findings show that the importance of each factor and how they influence the PE market in isolation are difficult to determine. Many of the factors are often highly correlated, and it is reasonable to believe that PE investors consider the combination of these factors, rather than evaluating each component separately, when analysing the external business environment.

7.3 Limitations of the Research

The empirical results reported herein should be considered in light of some potential limitations. Due to time constraints, the study only included the views of general partners of PE firms present in Tanzania. The inclusion of other stakeholders, such as limited partners could have shed more light, and provided a deeper understanding of the drivers that underpin the development of the Tanzanian PE market. It is also important to bear in mind the possible bias in these responses, as we excluded PE investors that have chosen *not* to invest in Tanzania, but in other less developed PE markets. This study sought to provide an understanding of the reasons for the low PE activity in Tanzania compared to other countries in its region. Therefore, it is reasonable to assume that the inclusion of these investors would provide a better explanation of the negative aspects of the Tanzanian PE market.

The second limitation concerns the lack of literature on the determinants of PE investments in emerging markets. Most of the existing literature for developing countries focus on early-stage investments, and most of the research for Tanzania only address issues concerning the development of FDI, which limits the depth of the study's literature review.

7.4 Suggestions for Future Research

There is abundant room for further progress in determining why Tanzania struggle to attract PE investments. Further research could be done by using comparative analysis to study the similarities and differences between the Tanzanian PE market and other similar PE markets. Future research may include comparing countries on the continent or the countries in the East African region. It is also recommended that future research includes the perspectives of limited partners and PE investors that have chosen not to invest in Tanzania.

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9. ATTACHMENTS

9.1 Interview Outline

Name of the business: Sector and industry:

QUESTIONS RELATED TO THE THEORETICAL FRAMEWORK

Question 1

How has the level of economic activities affected your decision to invest in Tanzania? how has the economic growth rate affected your decision? how has the employment level affected your decision? How has the degree of trade openness affected your decision? Are there any other factors related to economic activities that are significant to your investment decision?

Question 2

How did the depth of the capital market influence your decision to invest in Tanzania? How has the exit opportunities in Tanzania affected your decision? How has the size of the stock market and level of IPOs affected your decision? What about the opportunities for other modes of exits? How has interest rates and availability of debt affected your Invesment decision? Are there any other factors related to the depth of the capital market that are significant to your investment decision?

Question 3

How did the tax incentives and administrative burdens affect your decision? Can you explain how corporate tax rate and capital gains taxes have affected you. Was the time spent on tax issues a consideration? Are there any other factors related to the tax incentives and administrative burdens that are significant to your investment decision?

Question 4

How did investor protection and corporate governance affect your investment decision? How do you experience security of property rights and quality of legal enforcement in Tanzania? Are there any other factors related to the investor protection and corporate governance that are significant to your investment decision?

Question 5

How did the human and social environment affect your decision to invest in Tanzania? How are the conditions with the education, human capital and the labour market? Have bribery, corruption and the unofficial economy affected you in any way? What about the infrastructure? Are there any other factors related to the human and social environment that are significant to your investment decision?

Question 6

How did the entrepreneurial culture and deal opportunities in Tanzania affect your investment decision? How did the degree of innovation and ease of starting and running a business affect you? Are there any other factors related to entrepreneurial culture and deal opportunities that are significant to your investment decision?

OPEN QUESTIONS

Question 7

What is the least favourable and most challenging factors for PE investments in Tanzania, and how has this affected your investment decision?

Question 8

What factors make Tanzania an attractive country for PE investments and how has this affected your investment decision??

Question 9

How do you feel the investment climate, considering the mentioned factors, has changed over the years?

Question 10

Has there been any significant improvements for PE investments in Tanzania, and how has this affected the investment climate?

Question 11

Has there been any significant changes that has made it more challenging for PE investors in Tanzania, and how has this affected the investment climate?

Question 12

What do you consider to be the most important factors to improve in the years ahead to facilitate more private equity investments in Tanzania? (Short-term and long-term measures)

Question 13
What is your view of the private equity future in Tanzania?

9.2 Reflection Notes

9.2.1 Reflection Note 1

The aim of this study was to provide an understanding of the factors that could explain the low levels of private equity investments in Tanzania, based on interviews with different stakeholders of the PE industry in the country. The first objective was to identify and understand how different factors affect and determine the level of PE activity. The secondary objective of the study was to highlight the policy implications specific to Tanzania that could make the country a more attractive destination for PE capital. Tanzania has one of the highest economic growth rates in the African continent, but struggles to attract PE capital compared to its peers, especially in the East-African region. The decline in investments together with the changes after the recent presidential election in 2015, and a limited body of previous research on this field for Tanzania, made it an interesting topic to study. Our findings suggest that tax rates, availability of debt, quality of legal enforcement, human capital, deal opportunities, political stability, and investors' perception of a country are the most important factors that contribute to explaining the development of the Tanzanian PE market. The results of the study also indicated that there were five key areas in need of improvement in order to increase the country's attractiveness for PE investors; legal system, tax system, administrative burdens, education system, and infrastructure. It was emphasized that there is a need for an increased effort from the policymakers to focus on and improve these areas to increase investment activity and shift the recent negative trend.

In today's society there is an increased globalization and the barriers to investing in countries that are cultural and geographical distant has been lowered and are now less apparent. This means that more capital is spread around the globe and invested in areas that are distant and different to the host country. This is particularly relevant for many of the developing countries that have a short history of foreign investments that is not characterized as aid or provided by Non-governmental Organizations or Development Finance Institutions. Countries like Tanzania has recently in the last two decades experienced a steep growth in the inflow of capital from the commercial driven sector of PE firms and other similar organizations providing foreign direct investments. Before this period, it was deemed to risky and not profitable to invest in many of the least developed countries. The situation has now changed, and the increased internationalization has decreased the barriers of investing and allocating capital to a country like Tanzania. The opportunities of diversification of the investment portfolio to emerging markets for PE firms in recent times also means that an increasingly important step in the allocation process is evaluating the risks associated with entering the new market. The new ways of investing in markets which could be very different creates a stronger need for an overall assessment of the socio- and macroeconomic environment in the new country. In order to assess the attractiveness of different markets, investors often incorporate and analysis factors similar to those included in a PESTEL framework for an overall analysis initially. As more international and foreign investors are present or consider allocating capital and financing businesses in emerging markets there are a greater pressure on the local governments to facilitate changes that are conducive to investments. The provision of foreign finances are often a good source of economic growth and development for the least developed countries. It therefore means that the arrival and presence of PE firms, and the provision of capital from them in to new markets, will have a greater influence on the development of the country. The increased internationalization has in this case resulted in a situation where many of the large-scale PE firms from the developed parts of the world are providing financing to less developed countries like Tanzania, where it used to be mostly non-commercial organizations that would provide capital to the private sector. The development of poor countries is now more influenced by big players in the commercial sector of financing and we have witnessed an increased competition, among many of the poorer countries, to attract the capital of those players.

The PE, and especially venture capital sector are characterized by its promotion of innovation and financing of young and small enterprises. The presence of PE and VC investors means that there are financing opportunities for innovative and new businesses that regular financial intermediaries often would not even consider providing financing for. The problem is often that the potential investor and investee do not know of each other and the possibilities. In the case of Tanzania there is a lot of new businesses that are in need of financing, and also investors looking for new prospects that has the potential to grow and give them a return on their investments. However, it is often hard for both parties to get in touch and reach other due to lack of awareness and information, but also other factors such as geographical distance in the country where many lives in remotes areas and has limited access to internet or other means of communication. It might therefore be a need for innovation and new thinking in the aspect of connecting potential investors and investees across the country. One possible improvement could be increased effort from organizations in the private sector, PE firms and, the government to create a platform where entrepreneurs and investors are able to reach each other online as a way to connect with each other faster and also obtain information in a more efficient manner. There is of course the problem that many lack access to internet, but a growing part of the population are being connected to the internet in some way and it does not seem that this opportunity of creating a platform on this medium has yet been exploited properly. Both suppliers and those in demand for financing would benefit if there was a place with easy access to information and the possibilities that actually exist. An online platform developed by the stakeholders of the PE industry in Tanzania might fill that gap in the future.

The PE industry in Tanzania faces several ethical issues and challenges related to responsibility when investing in businesses in the country. A widespread culture of bribery and corruption together with other illicit practices from many businesses in the economy means that the PE firm needs to be extra aware of the operations of their investees and chose whether they want to support and finance businesses that participate in such practices. It could be tempting for many investors to ignore the actions of their investees as long as they have good returns and provide the investors with what they want. It is easy in this case to put the responsibility on the enterprises and the management of the business, and for the investors to only care about their returns. Investees that do not entirely operate within the legal framework or within a grey area might gain a competitive advantage which sees them grow faster and yield a better profit for their investors. However, foreign investors coming in to the country with a large amount of capital looking to invest in businesses needs to be aware of this problem and choose not to support those who participate in these illicit practices. There is a stronger need for an extra assessment of this in the due diligence process and also to follow up with the investees. The moral obligation of the investors to not exploit and earn money of businesses that is not contributing to a fair business environment should be emphasized internally in each of the investing firms and also serve as a guideline for those who wants to be a member of the PE industry in Tanzania.

9.2.2 Reflection Note 2

This study focuses on finding determinants of the private equity activity in Tanzania, and provide an understanding of how these factors affect the development of private equity.
In the last decade, the global private equity industry has experienced growth, but Tanzania has not been following the same trends, rather the country struggle to attract private equity investments. The secondary objective of this study was to highlight the policy implications specific to Tanzania that could make the country more attractive for private equity investments. A qualitative approach, where we interviewed actual private equity investors in Tanzania, was used to find the factors and how they affect the development of private equity in the country.

Our main findings from this study are that tax rates, availability of debt, exit opportunities, quality of legal enforcement, education and human capital, and deal opportunities are the most important factors that contribute to explaining the development of the Tanzanian private equity market. The importance of each factor and how they affect the private equity market in isolation are difficult to determine, because they are often highly correlated. Therefore, when analysing the external business environment it is important to consider the combination of these factors. There were also two new factors that emerged during the research; political stability and invertors' perception of a country that were perceived as important in the explaining of the Tanzanian private equity market. We also found that the policymakers need to focus on, and improve areas such as the legal system, tax system, administrative burdens, education system, and infrastructure to attract more investments.

In an increasingly globalized world where physical distances become less important, especially in the world of financing, private equity firms find interest in new markets. Internationalization is an important part of moving forward, and gives the possibility to geographically diversify and exploit opportunities in different parts of the world and markets with less history of PE financing. Snow, (2012), claims that globalization is one of the major trends in the PE industry, and has successfully facilitated private capital to flow across countries with little restrictions. Today, PE firms are helping their portfolio companies become more compatible while expanding their mediate borders. Internationalization makes it possible to transfer skills and knowledge across countries and markets more freely. Since the global financial crisis in 2008, PE firms have moved into emerging markets as they looked for more diversification within their portfolios. Developing countries on their part benefit from private capital flow because they possess limited domestic savings, and PE capital brings with them finance, managerial skills, technology and marketing expertise. Nevertheless, internationalization can also create some obstacles for investors, as there will be more competitors. This is a threat for smaller private equity firms that might struggle if they have to compete with larger firms and funds.

The business world is rapidly changing and to stand out from competitors, businesses have to be innovative and create value in times of economic change. PE investors look for new businesses to invest in, and as the competition increases, the investees must stand out. The businesses should increase their effort to innovate the processes and products to achieve revenue growth and improve profits. However, innovations to improve products and processes can be both expensive and time-consuming.

Private equity firms do not only offer financial support, but also strategic advice in order to improve recipients' financial performance. These are businesses that might have difficulties attracting financing from the bank sector because of their small size, young age, high level of uncertainties and informational asymmetries. Private equity firms have a responsibility to improve the overall performance, not only by providing capital but knowledge and training, so that the investees can continue to thrive after the exit. Private equity investments are structured over a 10-year horizon, and are made with a focus on capital gains upon an exit, which will happen through an IPO, secondary buyout or trade sales. However, there is a tendency for investors to only focus on high returns *prior* to exit without any interest in recipients' performance after exiting and in the long run. There is a risk that fund managers undertake risk investments that will only be beneficial in the short term when they are involved in management, and not after they have exited. This is an ethical challenge that could affect the overall sustainability of the invested firm. Therefore, it is important that private equity firms leave a positive impact on those who benefit from their funds and expertise after an exit.

Another important area with respect to responsibility is the fact that PE firms should invest in businesses that have a positive social and environmental impact. Corporations have a big impact on people's lives and the society, therefore it is important to hold businesses accountable for their actions. Corporate social responsibility is about following the lines of action which are desirable in terms of the values and objectives of our society. Therefore, private equity firms have an ethical responsibility to invest in companies that operates in an ethical manner. A private equity investor must evaluate several factors such as the company's financial statements, market position, and industry trends to determine whether investment is a good one, or not. However, it is equally important to incorporate an evaluation of the actions the investees are taking to be ethical and socially responsible.