

POLICY NOTE



**ZANZIBAR'S
ECONOMIC
TRANSITION:
IMPORTANCE OF
HARNESSING THE
OCEAN BASED
INDUSTRIALISATION**

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Introduction

Utilisation of the ocean-based economic activities is becoming increasingly important and also the most realistic pathway for enabling small island developing states (SIDs) to attain rapid economic and sustainable development. The harnessing of these particular frontier economic activities is gaining momentum in many SIDs which are characteristically lower middle income economies endowed by the ocean resources. Beyond being a leading contributor of a key life-support system for all life on this planet, the ocean-based economic activities provide livelihoods for more than 3 billion people worldwide; most of them live in developing countries. Ocean-based sectors are projected to create USD 405 billion and USD 576 billion, as well as 57 million and 78 million jobs by 2030 and 2063, respectively. Combined outputs of the key ocean-based economic activities are likely to outperform the general global economy (OECD, 2016). Each dollar invested towards the ocean economy typically yields, on average, five dollars in return.

In Zanzibar, consistent with the classical accounts of economic development, as the ocean economy continues to grow, more resources ought to be invested towards ocean-based industrialisation, where productivity is likely to be higher. Some emerging economic activities - such as offshore wind energy, growing aquaculture and marine biotechnologies - present a great option for robustly harnessing ocean-based industrial development. Yet, the ocean-based industrialisation has been negligible. Motivated by this reality, the main objective of this Policy Brief is to explore the most effective options for

harnessing marine based industrialisation in Zanzibar.

Why is it important to harness ocean-based industrialisation in Zanzibar?

The role of government support on backing domestic industries is gaining a growing importance across the globe. The concept of industrialisation is not an entirely new concept in Zanzibar. As other general industrialisation drives show signs of sparkling in the last decade and the existing unwavering political willingness to improve the enabling business environment, the push for ocean-based industrialization is looking increasingly possible. An industry is a relatively small sector in Zanzibar, yet is growing the fastest. As of the year 2021, for instance, the contribution of the industry sector as a proportion of gross domestic products (GDP) stood at 19.4%. It grew at an average rate of 6.2% between 2018 and 2021, which was significantly higher than the growth rate of 3.1% recorded by a combination of fishing, agriculture, forestry sectors over the same period.

A nationally defined strategic approach is being deployed by the government with notable progress in empowering the micro, small, and medium sized enterprises (MSMEs) across the strategic ocean-based sectors: fishery, seaweed farming and aquaculture. This includes the establishment of Zanzibar Economic Empowerment Agency (ZEEA), which was later merged with the Micro, Small and Medium Industrial Development Agency (SMIDA) and capitalised with about USD 7.5 million in the fiscal year 2022/23, to establish a revolving fund for empowering

local enterprises and small industries. Despite this a great push made by the government, the progress in ocean-based industrialisation has not been impressive.

How is the Financing of the Marine Based Industrialisation in Zanzibar?

Kick-starting the financing process by narrowing down types of industries to be developed from the strategic sectors across the ocean economy in line with over-reaching national policies and plans is crucial. Identification of strategies that aim to harness ocean-based industrialisation has already been done by Zanzibar Blue Economy Policy 2022. A remaining issue is how to accumulate and allocate funds in productive and profitable sectors of ocean-based industries in an economy without an efficient domestic capital market. State-Owned Enterprises (SOEs) are expected to deliver critical services in the industrialisation journey. Investments are being made to create national industrial champions such as Zanzibar Fisheries Company (ZAFICO) and Zanzibar Seaweed Corporation (ZASCO). But so far only ZASCO has translated into the actual operating industry.

Historically, and to this date, there is no large scale ocean-based industry which has been built in Zanzibar, despite the existing strong pro-private sector vision. The government commitment to bring marine-based industrialisation goes beyond just playing the harnessing role through policy measures to create an enabling business environment. This is demonstrated by a move to inject capital to ZASCO and ZAFICO. Nonetheless, financial economics theories and empirical analysis present evidence about the cautiousness of government

direct investments in business undertakings. The agency cost theory suggests that the separation of ownership and control are likely to cause SOEs to have incentive for making investments without feasible business models and risk adjusted returns. Factors in terms of perceived Zanzibar's unique riskiness of a systemic risk can also be contributing factors for the prevailing dearth of the private capital to finance ocean-based industrialisation in the country.

An Actual Ocean-Based Industrialisation Performance in Zanzibar

Industrial development is inherently a long-term process. Indeed, the ocean economy industrialisation process is often carried out through two main phases. The first occurs in short and medium terms through which industrial development efforts concentrate on building semi-processing and low technology based industries, preferably through private sector investments. During the second phase, the focus shifts into employing new technology, more knowledge and capital intensive, greater value addition industries in the areas of marine aquaculture, offshore oil and gas exploration and drilling, offshore wind energy, ocean renewable energy, marine and seabed mining, maritime safety and surveillance, marine biotechnology, and high-tech marine products.

Financing of Fisheries and Seaweed Industries

The establishment of ZAFICO perceived to be a major step for transforming the fisheries sector. It was expected to building

fish processing industries. The jury is still out if these ambitions would be realised and turn out to be profitable ventures. There are other small private companies carrying out deep sea fishing at a relatively small scale. All these companies, however, have not managed to industrialise the marine-based ocean economy. If fish processing industries can showcase the robustness of its potential risk adjusted return through convincing business models, then there is no reason why capital from private investors will not be directed to build fish processing industries as has been the case in the maritime transportation sector.

The government is continuing to finance ZASCO. The investment involves building a semi-processed seaweed processing factory to produce carrageenan in Pemba. Further, the government has offered boats to seaweed farmers through soft loans. The decision was intended to bring a positive effect on the general productivity of this sub-sector. Nonetheless, the direct causality to the volume of seaweed farming could be constrained by the small size and durability of boats given to seaweed farmers. A serious concern to the operationalisation of ZASCO semi-processing industry is the lack of predictable supply of 30,000 tons required by the factory to operate at full capacity.

Main Challenges constraining the Ocean Based Industrialisation

Power Accessibility: industries in Zanzibar are facing high costs of doing business due to shortage and unpredictable electricity. This problem is more acute in Pemba compared to Unguja. The utilisation of renewable energy from diverse sources is

deemed as an adequate solution. The new development in terms of the Power Purchase Agreement (PPA) between the state-owned entity known as the Zanzibar Electricity Corporation (ZECO) and private investors - i.e., Mauritius-based Generation Capital Ltd and Tanzania's Taifa Energy - to build its first large-scale plant (30MW solar PV solar power plant that will cost USD 140 million) in Unguja will help to reduce the cost of operating industries.

Limited capital - Zanzibar being small in size with limited capital markets can be attributed to be among major reasons for a sluggish process of marine based industrial development. This can explain the inability of local investors to invest in large industries.

Climate Change Vulnerability - This is a persistent and growing threat to almost all SIDs' economies. Rising temperatures and floods could possibly have a detrimental impact on the ocean-based industrialisation in Zanzibar.

Infrastructure development – A road network is being created across both main islands of Zanzibar. In the next few years all parts of Unguja and Pemba will be connected by roads. The maritime is the most prominent means of transportation and has enabled Zanzibar to be a trade hub since many centuries ago. It accommodates over 98% of international based trades. Nonetheless, port congestion was among the biggest shipping problems facing ocean-based industrialization in Unguja, whereas in Pemba the challenge is the absence of a shipping port. A deal between the government and Africa Global Logistics (AGL) for the management of the Malindi Container Terminal is expected to

modernise cargo handling operations. This agreement has started to lessen cargo congestion at the port, but a permanent solution lies on the construction of a multipurpose and large port at Mangapwani.

The air transportation in Unguja is in a good shape to support ocean-based industrialisation. The Karume International Terminal II is a world class international airport. On the contrary, the airport in Pemba is not at an international standard to faster business movements that are typically attached to industrial development, but the government of Zanzibar has signed a USD 230 million contracts to upgrade Pemba Airport to become International status, and upon completion the new airport will have the capacity to serve 750,000 passengers per year.

Technology - This is among both main preconditions and leading driving forces for industrialisation as it makes production faster, simpler, and more efficient. However, the move to use technology to operationalise ocean-based industrialisation will be complex, especially due to apparent low ICT and digital skills, but a necessary undertaking. An embracement of ICT and emerging technologies needs to be among main drivers of the ocean-based industrialisation in Zanzibar.

Experiences from the Developed Ocean-based Economies

Norway and Iceland are among leading ocean dependent nations and the second and third largest fish catch in the northeast Atlantic sea, respectively. They provide an excellent illustration on how marine based

industrialisation can be smartly be used to bring economic development. Ocean-based industries (oil and gas, shipping and seafood), for instance, account for about 70% of Norway's export earnings and provides 11% of all employment in the private sector, and in 2017, total value creation in the ocean industries was about USD 680 billion, which means that the ocean industries account for more than 30% of all value creation in the private sector, as demonstrated by the Norwegian Ministries Strategy, 2020.

In Iceland, the economy is using technology led innovation and digital applications to industrialise almost all ocean related economic activities. According to the International Monetary Fund (2018), Iceland has the third largest fish catch in the northeast Atlantic, after Russia and Norway. By volume, its total catch amounted to over 1.1 million tons, and the largest buyer is the United Kingdom, which takes a big share of Iceland's fish catch, followed by Spain and France. What is impressive about Iceland is that value added has been lifted by advances in fish processing. Iceland's fishing companies have invested in state-of-the-art technologies to link fishing with processing. Plants processing fresh and frozen products operate in various parts of the country, focusing on ground fish, pelagic, or roe, with the pelagic plants also processing fishmeal and oil. Large freezing vessels also process catches on board, allowing them to land finished products. Most of the large fishing companies are vertically integrated, covering fishing, processing, and marketing.

Conclusion and Specific Policy Recommendation

The on-going move to leverage on the ocean economy for attaining the prosperity of Zanzibar is well perceived by both local and foreign investors. There is a perception that the ocean-economy is well positioned to become a lucrative sector with a potential attractive huge pay off. However, only limited progress has been in the industrialisation of the ocean-based economy. To kick-start and make a rapid progress of ocean-based industrial development, many practical oriented activities and policy measures will need to be undertaken. Policy-makers' role in harnessing marine-based industrialization is notable, but there are areas for improvement. It includes addressing policies and regulatory concerns in terms of excessive government investment, import rules, complex licensing, exportation regulations, and an enabling business environment. Given the existing small size of the private capital, the selection of one sector between fisheries and seaweed to be the frontier for industrialising the marine economy, is *the elephant in the room that needs to be addressed calmly*.