East African Journal of Business and Economics, Volume 8, Issue 1, 2025
Article DOI: https://doi.org/10.37284/eajbe.8.1.2673

East African Journal of Business and Economics
eajbe.eanso.org
Volume 8, Issue 1, 2025
Print ISSN: 2707-4250 | Online ISSN: 2707-4269
Title DOI: https://doi.org/10.37284/2707-4269

EAST AFRICAN NATURE & SCIENCE ORGANIZATION

Original Article

The Role of Value-Added Tax Revenue on Gross Domestic Product (GDP) in Tanzania

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Article DOI: https://doi.org/10.37284/eajbe.8.1.2673

Date Published:

05 February 2025

Keywords:

Value Added Tax, Nominal Gross Domestic Product.

ABSTRACT

The objective of this study is to examine the role of Value Added Tax (VAT) on the nominal GDP in Tanzania. The study adopted ontology philosophy and quantitative descriptive design. This study used only secondary data which was collected from the Tanzania Revenue Authority (TRA) and Bank of Tanzania financial stability reports for the period of 2015 to 2022. The data was analyzed quantitatively through descriptive statistics and linear regression. The study findings revealed that the VAT revenue collected by TRA has a significant contribution to the growth of the country's GDP. When VAT increases by 1 unit, the nominal GDP increases by 9.56348 units and the P- value is less than 5% which indicates statistical significance. The regression results are supported by the descriptive statistics whereby, from 2015 to 2022, domestic VAT and Import VAT were increasing at an increasing rate. This study recommends that the Tanzania Revenue Authority should take all necessary measures to reasonably reduce the VAT rate from 18% to promote the production and supply of goods and services in the market by the existing manufacturers since such a reduction of VAT rate will lead to the reduction of production costs. The reduction of the VAT rate may also lead to an increase in the rate of voluntary tax compliance and a decrease in the prices of goods and services that ultimately boost the consumption of goods and services in the economy. It is further recommended to the government of Tanzania, specifically, the Ministry of Industry, Trade and Investment to improve and further promote its investment policies to attract Foreign Direct Investments (FDIs) into the manufacturing sector since VAT is an input tax and it is charged into the value addition of products during different phases of manufacturing. Thus, growth of the manufacturing sector in the country will mean growth of VAT revenue collections and ultimately GDP growth.

APA CITATION

Nguvava, H. E. & Bandile, L. E. (2025). The Role of Value-Added Tax Revenue on Gross Domestic Product (GDP) in Tanzania. *East African Journal of Business and Economics*, *8*(1), 85-95. https://doi.org/10.37284/eajbe.8.1.2673

Article DOI: https://doi.org/10.37284/eajbe.8.1.2673

CHICAGO CITATION

Nguvava, Heriel E. and Lusubilo Enock Bandile. 2025. "The Role of Value-Added Tax Revenue on Gross Domestic Product (GDP) in Tanzania". *East African Journal of Business and Economics* 8 (1), 85-95. https://doi.org/10.37284/eajbe.8.1.2673.

HARVARD CITATION

Nguvava, H. E. & Bandile, L. E. (2025) "The Role of Value-Added Tax Revenue on Gross Domestic Product (GDP) in Tanzania", *East African Journal of Business and Economics*, 8(1), pp. 85-95. doi: 10.37284/eajbe.8.1.2673.

IEEE CITATION

H. E., Nguvava & L. E., Bandile "The Role of Value-Added Tax Revenue on Gross Domestic Product (GDP) in Tanzania", *EAJBE*, vol. 8, no. 1, pp. 85-95, Feb. 2025.

MLA CITATION

Nguvava, Heriel E. & Lusubilo Enock Bandile. "The Role of Value-Added Tax Revenue on Gross Domestic Product (GDP) in Tanzania". *East African Journal of Business and Economics*, Vol. 8, no. 1, Feb. 2025, pp. 85-95, doi:10.37284/eajbe.8.1.2673.

INTRODUCTION

The cardinal purpose of any taxation is to supplement the government to acquire funds for carrying out functions accorded to it (Oluwasegun, 2022). This is based on the reasoning that taxation is a vital tool in generating revenues for states with scarce resources (Hlongwene, 2022). Thus, the need for governments to have a broader source of revenue from taxation led to the adoption of VAT. VAT as a tax policy was imposed on products in regards to the value-added on the said products based on the chain of production the particular product passes through (Lalarukh, 2013). This is to ensure that each stage is taxed and the consumer pays the VAT indirectly. In some states such as Bahrain, VAT on products is taxed at a rate of 5% percent (Bansar, 2023) while in some states as Sweden their VAT amounts to 20 %. VAT is directly associated with the economic growth and development of a state (Shakkar, 2020) and that is why it is important to stress the compliance of VAT so that the yields may be felt by the government taxing authorities. For example, in Saudi Arabia, the VAT began its implementation at a small rate of 5 % percent though being of a smaller rate the VAT has a positive effect on the GDP of Saudi Arabia (Bogeri, 2020).

In practice, VAT has become the third source of revenue for various states of the world (Bhandari, 2015) this is because VAT is a convenient tax, which is indirect and based directly on the registered VAT taxpayers for tax liability (Shiva, 2021). Thus, the registered VAT taxpayer has the legal obligation to pay the stated VAT to the taxing authorities. Thus, the VAT collections are obtained from the VAT-registered taxpayer and convenience in the payment of VAT as from the VAT rate is very essential. Although VAT is a consumption tax on goods and services based on what consumers may consume, the tax liability is not upon the consumer but the registered taxpayer (Herbain, 2020). This is because VAT is essentially imposed on each value added in the production process, thus making the manufacturer have tax liability at any stage of production (Msangi, 2015). Therefore, to yield the revenue from the VAT the taxing authorities need to identify the tax base of VAT and the VAT-registered taxpayers present. However, it can be said that the administration of VAT is not that severe as the evasion of tax is at a lower rate and it allows equity (Orisadare, 2022). These two factors make it easy for administration and attractive to apply in a domestic tax regime.

The presence of VAT has led to an increase in the national businesses and industrial sectors (Qingzi, 2021). This is an undeniable truth because globally VAT generates more than 20% of the global tax revenue (Johnson, 2020), although, the revenue collections from VAT in many jurisdictions may vary. After all, each state shall have its rate of VAT and different tax base. In some Jurisdictions such as Nepal, the trend between VAT and total revenue of the state has been promising (Dahal, 2020). In many jurisdictions, VAT has been taken as a foreign mechanism adopted for the application in their

Article DOI: https://doi.org/10.37284/eajbe.8.1.2673

domestic tax regime (Siems, 2015). For example, in Nigeria, the VAT was introduced in 1994 to take over the repealed sales tax which was characterized by shortcomings (Abimbola, 2021). After its introduction in 1994, it imposed a rate of 5% but as of 2020, the rate was increased to 7.5% rate (Oluwasegun, 2020). Though it is a foreign-adopted tax policy, VAT has been generating income for the government of Nigeria (Oseni, 2016). This has not left behind regional cooperation such as the EU which has established a 12% VAT rate to be the minimum within its member states (Maganga, 2020) and the Gulf Cooperation which imposed a 5% VAT rate to its members to meet the oil prices deficit

In a global context, the origin of VAT has faced tremendous debate as its origin is based on conflicting views one side states that the VAT originated from an American scholar Thomas Adams and others group argue for VAT to be an innovation by a German Scholar named von Siemens (Agbo, 2020). All in all, the presence of the innovation of VAT must be greatly accredited to the above two scholars as founders of VAT that is Von Siemens and Thomas Adams (Mahangila, 2016). But as to the context of this study, it is based on the side of the American scholar Thomas Adams as the origin of VAT. This is because, after the First World War, the government of the USA was in demand of a policy to deal with an economic depression brought about by the WW1 (Mahratta, 2022). This need for a new policy gave rise to the American Economist Thomas Adams to come up with a draft tax proposal that could do away with the economic depression of the USA, by proposing a Federal Consumption Tax which we apply today as VAT (Mahratta, 2022).

Although VAT is not a recent phenomenon, as it was traced in the 1920s from the works of Thomas Adams, it gained its prominence in the 20th Century (Agbo, 2020). The first jurisdiction to apply VAT was the Republic of France in the year 1954 but in a limited application, until 1968 when it was fully applied (Agbo, 2020). The second state which followed France to apply VAT was the state of Denmark in the year 1967. It can be argued that the VAT began application in Western Europe in the 1960s. As of Current, there has been a drastic adoption of VAT by states from the 1980s to the 1990s, especially after the fall of the Berlin Wall and the breakaway of the Soviet state (Ajay, 2019). The adopted VAT became a great contributor to government revenue for states which adopted it (Ufer, 2014). This is to say many economies have adopted VAT thus making it an important tax mechanism in their jurisdictions (Manning, 2015). For example, many states of the world have their VAT rate such as Bulgaria at 20 %; Bosnia at 1%; Cambodia at 10%; Cameroon at 19.5%; Ghana at 12.5 %; France at 20%; Greece at 24%; Moldovia at 20%; Nigeria 7.5%; Kenya 16% and Tanzania 18% (Milon, 2023)

In an African Context, many African states introduced VAT during the 1990s and in the early 2000s (Chindegwile, 2022). For example, Algeria established VAT in 1992; Benin established VAT in 1991; Ethiopia established VAT in 2003; Ghana established VAT in 1998; Egypt established VAT in 1991 and Chad established VAT in 2000. The range of VAT rate among the African States is between 18% the highest rate and 8 % rate at the lowest rate of VAT (Oseni, 2016). The basis of adopting VAT in many African Jurisdictions was to meet the economic struggles that face them such as public debts and poverty (Mwakalobo, 2021). Thus, in the economic struggles of the African states, VAT comes in as a tool to enable states to raise their revenues. However, during their immediate adoption of VAT in their jurisdictions, the African states were faced with consumption challenges for their citizens who could not purchase certain goods and services as their prices were affected by the VAT rate (Bansar, 2023). Thus, for the VAT to accomplish its purpose, the African governments are required to ensure it is properly administered so that the intended revenue targets are met. This is the most important factor for the realization of VAT.

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In terms of GDP, being an essential tax mechanism, VAT has become a major booster to various African economies in terms of GDP (Hlongwene, 2022). There is an important relationship between VAT rates and the GDP of a state. It is important to note that the imposition of VAT in any jurisdiction has a drastic effect on the growth of the GDP of a state (Milon, 2023). This is because VAT is imposed on the consumption of goods and services for an increase in government revenues (Gurder, 2021). For example, the Republic of South Africa, one of the strongest economies in Africa, has maintained its VAT rate at 14% from the year 1992 to 15% as of 2018 (Hlongwene, 2022). The presence of VAT has had a great contribution to the nominal GDP of South Africa, whereby the VAT has contributed 25% of the total revenue of South Africa and 6% of the nominal GDP of South Africa (Hlongwene, 2022). Thus, VAT can be said to have a great contribution to the GDP of South Africa (Erero, 2021). Thus, African states have been trying to maintain VAT-to-GDP ratios. For example, the states of Zambia, Mauritius, Botswana, South Africa and Cape Verde had an 8 % contribution of VAT to the GDP (Erero, 2021). The tax to GDP ratio has been promising as often studies have been utilizing Tax revenues to contribute to their GDPs.

In a Tanzanian Context, VAT was established in 1993 just after economic liberalization came into force. The Presidential Enquiry Tax Commission of 1991 came up with proposals on government revenues and expenditures (Fjelstad, 2017) with VAT being one of the proposals of the Commission. In the proposal for VAT, the Commission proposed that there was a need to tax manufacturers and importers (Fjelstad, 2017). Thus, since 1993 VAT has been in operation with the basic motive of widening the tax base and increasing the revenues for the government. The application of the VAT has been very essential in Tanzania, as the state is moving to be an industrialized economy and intends to establish a stable manufacturing sector. Therefore, the more the manufacturing industry is booming, the more there is assurance that VAT shall lso do well as the manufacturing industry is the best stakeholder for VAT (Chindegwile, 2022). This means, that the more the industries prevail in Tanzania then the more the revenues from VAT shall be accrued.

Despite being the second-strongest economy in the East African Community, Tanzania has not fully leveraged its VAT system to optimize economic benefits. While the country's GDP has shown steady growth, increasing from USD 61.026 billion in 2019 to an expected USD 75.073 billion in 2023 (NBS, 2023), the precise role of VAT revenue in this economic expansion remains unclear. The disconnect between rising GDP and uncertain VAT contribution raises critical questions about the effectiveness and efficiency of the VAT system in Tanzania. Previous studies have highlighted the importance of VAT in other African nations, where it constitutes a significant percentage of GDP. For instance, Rwanda’s tax revenues contribute 17% to its GDP, while Mali’s tax revenues contribute 19.7% (Chindegwile, 2022). Yet, the question remains whether Tanzania is achieving similar outcomes or if there are inefficiencies in its tax collection and administration processes.

As of the current status, the economic growth of Tanzania is projected to grow at a rate of 7.1% (NBS, 2023), even though there were economic hardships brought forth by the Russia and Ukraine war (Nguvava, & Athanas, 2023), this proves that Tanzania is prospecting to be a great economy in the future. Thus, having a proper tax regime as VAT shall be of merit as it shall bring forth more revenues to the government and stimulate further economic growth. According to the Bank of Tanzania, the GDP growth in Tanzania was at a rate of 5.7% in 2023. (BOT, 2023). But as it can be noted, the main contributors (sectors) in the Tanzanian economy have been agriculture, construction and mining and not manufacturing. Thus, there is of high need to establish whether the VAT as an essential tool for government revenue has a significant contribution

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to the GDP of Tanzania and offer appropriate recommendations.

METHODOLOGY

Research Philosophy

The research philosophy guiding this study is primarily aligned with the ontology paradigm. Ontologists emphasize the objective observation of phenomena and the application of scientific methods to gather empirical evidence. A positivist approach is chosen due to its suitability for quantitative analysis and the establishment of causal relationships.

Research Design

The quantitative descriptive design was employed by the researcher so as to obtain the required data for the study and facilitate quantitative analysis. The quantitative approach enabled the researcher to test hypotheses and arrive at specific conclusions that can be generalized. A longitudinal strategy was also adopted since the data were time series.

Research Area

The study was conducted in Tanzania's Mainland. The GDP data and VAT revenue collection data (Domestic and import) were obtained from the Bank of Tanzania and TRA headquarters for the period of 2015-2022 and suffice the need for study.

Data Collection Methods

This study used secondary data only. The data was obtained through a documentary review. Data was extracted from TRA revenue collection reports and Bank of Tanzania reports for the study period and further complemented by data from the National Bureau of Statistics. All the data collected was time series in nature.

Data Analysis, Interpretation and Presentation

Data was coded and analyzed quantitatively by using STATA software. The first, second and third specific objectives were analyzed through the ordinary least square method. Tables and figures were used to present the research findings. The study used simple linear regression analysis to determine the cause-and-effect relationship between independent and dependent variables. The model is estimated as;

GDP= b +Xvat+ e

Whereby;

GDP stands for a dependent variable which is the Nominal Gross Domestic Product

B stands for the constant term/coefficient of the model

Xvat stands for an independent variable (Total Value Added Tax)

e stands for an error term

Reliability and Validity Analysis

This study applied the unit root test (ADF test) to measure and ensure stationarity of data. Cronbach's alpha was used to test the reliability coefficient, which calculates internal consistency by examining how each test item relates to each other and to the entire test., where "_ > .9 – Excellent, _ > .8 – Good, _ > .7 – Acceptable, _ > .6 – Questionable, _ > .5 – Poor, and < .5 – Unacceptable". Cronbach's alpha reliability coefficient, given as a value between 0 and 1, was employed in this study. The scale's items may be internally consistent when Cronbach's alpha is close to 1.0.

RESULTS AND DISCUSSION

Reliability Test

The study applied Cronbach's Alpha coefficient to test the fitness of the instrument of the study to give the desired results. In the table below, it was revealed Cronbach's alpha coefficient of 0.8936 which is above 0.7, thus it has been concluded that there is internal consistency in the data set and that the data used is reliable.

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Table 1: Results from Cronbach's Alpha Test

Description of item	Results
Observations	8
Test scale	Mean (Standardized item)
Number of items in the scale	2
Scale reliability coefficient	0.8936

Source: Author (2024)

Stationarity test

The unit root test was used to determine the properties of the variables for the period under study 2015-2022. The Augmented Dickey-Fuller unit root test was used to measure the presence of unit root. Table 2 is the output of the test.

Table 2: Unit Root Tests

Variables	ADF		
	t-statistic	Prob	Order
Nominal GDP	2.326	0.9993	I(1)
Total VAT	0.222	0.9877	I(1)

Source: Author (2024)

From Table 2, the output of the unit root tests using the Augmented Dickey-Fuller (ADF) shows that all the variables were stationary at the first difference I (1).

Descriptive Statistics

Descriptive statistics describes the variables used. The section provides the statistical characteristics of data on the VAT Revenue collection and the GDP in Tanzania. From Table 3 and Table 4, the Value Added Tax Revenues have been increasing at a percentage rate of 9.25% for VAT on imports and 8.3% for domestic VAT respectively. In general VAT collections have been increasing for the period from 2015 to 2022. It was noted that in the year 2021, the VAT Revenues on domestic goods and services in the United Republic of Tanzania Decreased by 4% rate, although this slip in the VAT revenue collection did not affect the overall VAT revenue growth for the period between 2015 to 2022 as the total mean for the domestic VAT revenue growth was positive at 8.3%. The total increase of the VAT revenues for the eighth year indicates that there is a positive relationship between the increase in VAT Revenues and the GDP in the United Republic of Tanzania and that the VAT Revenues have a positive effect on the GDP in the country.

Table 3: VAT on Imports (USD Millions)

VAT	2014/2015	2015/2016	2016/2017	2017/2018	2018/2019	2019/2020	2020/2021	2021/2022
VAT on Imports	587.80	657.97	687.11	782.73	860.89	922.43	984.55	1274.21
Growth%	7%	10.6%	4%	12%	9%	6%	4%	22%
Mean	9.25%							

Source: (Author, 2024)

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Table 4: Domestic VAT (USD Million)

VAT	2014/2015	2015/2016	2016/2017	2017/2018	2018/2019	2019/2020	2020/2021	2021/2022
Domestic VAT	575.96	701.21	822.30	924.30	954.45	1052.54	1003.21	1124.92
Growth%	7%	17%	14%	11%	3%	9%	-4%	10%
Mean Growth	8.3%							

Source: (Author, 2024)

The GDP in Tanzania has been growing from year to year as revealed in Table 5 thus bringing a positive indicator on the economic growth within the United Republic of Tanzania. The GDP Nominal in Tanzania has been increasing at a mean rate of 5.3 percent and in 8 years the GDP Nominal has increased from 47.41 USD billion in 2015 to 75.73 USD billion in 2022. These findings complement the findings by the National Bureau of Statistics (2023) that projected the economic growth rate of Tanzania at 7.1% despite the economic hardships brought forth by the Russian and Ukraine wars.

The findings indicate that Tanzania is prospecting to be a great economy in the future. This has been associated with having Value Added Tax in place as it brings forth more revenues into the government and stimulates further economic growth. Thus, Value Added Tax has a direct connection to GDP. It has been noted, that the main sectors that contribute to the GDP in Tanzania have been agriculture, construction and mining. Thus, there is a need to stimulate the growth of the manufacturing sector since VAT is an input tax and it performs better where the manufacturing sector is highly performing.

Table 5: Nominal GDP (USD Billions)

GDP	2015	2016	2017	2018	2019	2020	2021	2022
Nominal GDP	47.41	49.77	53.27	57.00	61.03	66.07	70.66	75.73
GDP Growth	6.16%	6.87%	6.75%	5.50%	5.80%	3%	4.32%	4.56%
Mean Growth	5.3%							

Source: Author (2024)

Regression Analysis

The summary of the regression analysis between Total VAT (independent variable) and Total nominal GDP (dependent variable) is given in the table below;

Table 6: Summary of Regression Statistics

Multiple R	**0.978411**
R Square	0.957288
Adjusted R Square	0.95017
Standard Error	2.258136
Observations	8

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	16.44703	3.849555	4.27245	0.005249	7.027509	25.86655	7.027509	25.8665502
Nominal GDP	9.56348	0.824692	11.59643	2.47E-05	7.545531	11.58143	7.545531	11.5814284

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R-squared (0.957), indicates that 95.7% of the variation in Total GDP can be explained by the Total VAT. This high value suggests a very strong fit of the model to the data, meaning that VAT is a significant predictor of GDP in this context. Adjusted R-squared (0.950), the adjusted R-squared accounts for the number of predictors in the model. In this case, it's slightly lower than the R-squared but still indicates a strong model. Intercept (16.44)**,** this represents the expected value of GDP when VAT is zero. While a VAT of zero might be unrealistic in practice, the intercept provides a baseline for the model. Total VAT (9.56), the coefficient for Total VAT indicates that for every unit increase in VAT, GDP increases by approximately 9.56 units. This suggests a strong positive relationship between VAT and GDP, implying that as VAT revenue increases, the GDP tends to grow significantly.

The p-value for the intercept (0.0052) indicates that it is statistically significant at conventional levels (e.g., 5%). The p-value for the VAT coefficient (0.0000) is extremely small, showing that the relationship between VAT and GDP is highly significant. The t-statistics for the intercept is 4.2724, indicating that it is significantly different from zero. The t-statistic for the VAT coefficient is 11.59, suggesting very strong evidence against the null hypothesis. The 95% confidence interval for the VAT coefficient ranges from 7.53 to 11.57. This narrow range further indicates the precision of the estimate, giving confidence that the true effect of VAT on GDP lies within this interval.

The model suggests a strong positive relationship between VAT and GDP, meaning that as VAT increases, GDP also increases significantly. The p-values indicate that both the intercept and the slope are statistically significant. These findings highly complement the work by (Oluwasegun, 2022) that made an insight into the impact of VAT on the economic growth of Nigeria. He concluded that, after reviewing the VAT accounts in Nigeria, VAT had a significant contribution to the economic growth of Nigeria. This means that, as the VAT collections in Nigeria increase leads to further growth of the country's GDP. Thus, this study affirms a strong and positive relationship between economic growth and VAT especially in developing countries like Tanzania. The findings also confirm the work by Onakya (2017) who established that there is a relationship between taxation and economic growth in African states. He stressed that the contribution of taxation in the African economies is proportionate to the growth of the GDP in those economies.

This study finding is further complemented by the work of Hlongwene (2022) who suggested that the presence of VAT has a great contribution to the nominal GDP of South Africa, whereby the VAT has contributed 25% of the total revenue of South Africa and 6% of the nominal GDP of South Africa. Thus, VAT has a great contribution to the GDP of South Africa as it has also been confirmed to have a significant contribution to the GDP of Tanzania. The study by Odo in 2022 has highlighted the importance of VAT in other African nations and complements the findings of the current study. The study suggested VAT constitutes a significant percentage of GDP for most African nations. For instance, Rwanda's tax revenues contribute 17% to its GDP, while Mali's tax revenues contribute 19.7% (Odo, 2022) and a significant proportion of their tax revenue comes from VAT.

CONCLUSION AND RECOMMENDATIONS

Conclusion

The objective of the study was to examine the role of VAT on the growth of the GDP in Tanzania. This study adopted quantitative descriptive design which facilitates the apprehending of knowledge through measurements of phenomena by using statistical procedures. The study used a quantitative approach and longitudinal strategy to provide statistical evidence of the cause-and-effect relationship between the main variables of the study. Secondary data for VAT revenues for the period (2015-2022)

Article DOI: https://doi.org/10.37284/eajbe.8.1.2673

was retrieved from the TRA Databases while GDP data were obtained from the Bank of Tanzania (BOT) Quarterly Financial Stability Reports 2015-2022.

The findings revealed that the Value Added Tax Revenues have been increasing at a rate of 9.25% for imports and at a rate of 8.3% for the domestic VAT respectively. This means that the revenue flows of VAT in general have been increasing for the study period from 2015 to 2022. The GDP Nominal in Tanzania has been increasing at a mean rate of 5.3 percent and in 8 years the GDP Nominal has increased from 47.41 USD Billions in 2015 to 75.73 USD Billions in 2022. The increase in percentage in both VAT and GDP has been a strong indicator of a positive relationship between the VAT revenues and the GDP in the United Republic of Tanzania as confirmed by the regression findings which were positive and significant.

Recommendations

From the study findings, it is recommended that the Tanzania Revenue Authority should take all necessary measures to reasonably reduce the VAT rate from 18% to encourage an increase in the production of goods and services in the market by the existing manufacturers since such reduction of VAT rate will lead to the reduction of production costs. The reduction of the VAT rate may also lead to a decrease in the prices of goods and services and ultimately increase in the consumption of goods and services in the economy. It is further recommended to the government of Tanzania, specifically, the Ministry of Industry, Trade and Investment to improve and further promote its investment policies to attract Foreign Direct Investments (FDIs) into the manufacturing sector since VAT is an input tax and it is charged into the value addition of products during different phases of manufacturing. Thus growth of the manufacturing sector in the country will mean growth of VAT revenue collections and ultimately GDP growth.

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