Enhancing Resource Allocation to Urban Development in Africa


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UNITED NATIONS HUMAN SETTLEMENT PROGRAMME
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PREFACE

During the Third International Fair and Congress of Cities (URBIS III) held in Sao Paulo, Brazil, from 14-18 June 2004, UN-HABITAT organized a seminar on Cities-Engines of Economic Development. The objective of the seminar was to identify, underline and share experiences on the significance of cities to national and regional economic and social development and to discuss the sources of financing urban development and management within the context of an increasingly urbanizing world. UN-HABITAT has subsequently published a monograph entitled Cities – Engines of Economic Development, containing a few selected papers presented at the seminar.

As a follow-up to this monograph and to further enhance the importance of allocating adequate resources to urban development and management in Africa, UN-HABITAT organized an African Regional Seminar on Enhancing Resource Allocation to Cities to Strengthen their Role as Engines of Economic Growth and Development. The seminar was held in the UN Complex in Nairobi from 2 to 3 November 2005. The main objective of this regional seminar was to promote awareness among and to sensitize African policy-makers – notably in the planning, budget or finance ministries and departments – of the need to enhance resource allocation to African cities as a means to accelerating national economic growth and development, generating greater employment and increasing incomes. This report documents the proceedings of the seminar.

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INTRODUCTION

Cities are engines of economic growth and social development, drawing in human resources, raw materials and capital which, combined with more sophisticated urban infrastructure, have been the driving force behind national economic development in both developed and, increasingly, developing countries. Many recent country studies in all developing-country regions conclude that “cities, especially bigger cities, mean higher productivity and higher per capita incomes.” For economists this is not surprising, given that cities provide the economies of scale and agglomeration, as well as the socio-economic infrastructure, necessary for the acceleration of national economic growth and social development.

This central role played by cities in socio-economic development has been increasingly recognized in Africa, where greater allocation of resources to urban areas could offer a much-needed platform for creating wealth, attracting investment and employing human and technological resources to increase national productivity and competitiveness. This explains why UN-HABITAT has decided to take the initiative to convene a regional seminar to explore prospects of enhancing the capacity of African cities to accelerate national economic growth throughout the continent.

The African Regional Seminar on Enhancing Resource Allocation to Cities to Strengthen their Role as Engines of Economic Growth and Development – convened by the Urban Economy and Finance Branch of UN-HABITAT and held in Nairobi on 2-3 November 2005 – was attended by national government policy-makers, notably those belonging to finance, budget and planning ministries; urban development planners and municipal managers or administrators; researchers and practitioners dealing with urban development and municipal finance; members of the media specializing in urban development and municipal finance; as well as representatives of the private sector and civil society.

This report draws on the main papers, discussions and recommendations of the seminar to shed some light on the required measures to enhance resource allocation for accelerating urban development in Africa. The seminar attempted to fulfill this objective primarily through the fruitful exchange of ideas arising from four substantive presentations.

The first presentation draws upon Prof. Cohen’s paper entitled “Cities and the Wealth of Nations” to identify the major challenges to enhancing the role of cities as levers of national growth and economic development. In this regard, three key issues identified in the paper are examined in the following three presentations, namely (a) a more effective mobilization of public finance, (b) greater private sector participation and (c) the provision of incentives to improve the operational efficiency of the informal sector and increase its contribution to urban economic growth and development.

In the second presentation, Prof. Mosha explored how African countries have fared in mobilizing public finance for city and municipal development through public finance. The presentation examined the challenges these governments were facing and how these challenges could be overcome. The discussion produced innovative ways of mobilizing municipal finance for urban development.

In the third presentation, Mr. Nabutola examined the challenges and opportunities for greater private sector involvement in urban development and discussed different modalities of public-private partnerships, such as sub-contracting, leasing, concessions and privatization. The seminar participants agreed, however, that the level of private sector involvement should be determined by a city’s own needs for investment and technical capacity, paying due attention to the interests of lower-income urban dwellers.

In the last presentation, Mr. Okunlola stressed the critical role of the urban informal sector and micro-enterprises in job creation, income generation and broad-based economic development. The presentation also identified the major challenges and incentives for

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2. Contained in a recently-published UN-HABITAT publication and reproduced in Part II of this report.
informal sector development. The debate revolved around the presenter’s warning that any “city or state which does not have the goal of providing greater opportunities to the informal sector as a primary objective...is likely to only remain grounded in the mire of underdevelopment.”

Drawing on the excellent presentations and fruitful discussions, the report proposes several policy recommendations in the areas of public and private finance, as well as other key areas, such as the informal sector and reliable data availability. The recommendations are ultimately aimed to promote awareness among, and thus sensitize, African decision- and policy-makers – notably in the planning, budget or finance ministries and departments – of the need to enhance resource allocation to key African cities as a means of accelerating national economic and social development.
PART I. PROCEEDINGS OF THE MEETING

Objective of the Seminar

As concluded in a *State of the World’s Cities* report published by UN-HABITAT at the beginning of the new millennium, the “urban economy is the hub and nerve centre of the national economy and, as the global society expands, a nation’s welfare will be determined increasingly by the roles its cities play in the global economy.”

This prediction is not surprising, considering that the world’s economic history during the last century showed that the processes of urbanization and economic progress tend to be mutually reinforcing. The experiences of most developing countries during the twentieth century showed, in particular, that urbanization was closely associated with increasing levels of economic growth, income and social progress. For example, a comprehensive study of 90 countries from 1960 to 1980 provides evidence that the urban share of the population increases with national income per capita.

However, despite the widespread evidence that cities are engines of economic and social development, it is also surprising that “the urban share of the national economy ... is rarely recognized in global debates about economic and development policy.” There is now evidence to show, for example, that urban economic activities account for more than half of Gross National Income (GNI) in all countries, and up to four-fifths or more in more urbanized countries in Latin America, Asia and the developed world.

While the African continent is characterized by a broadly different picture, a certain degree of convergence with other regions is beginning to be experienced with regard to key cities in several countries in the eastern, northern, southern and western Africa sub-regions, such as Addis Ababa, Cairo, Cape Town, Casablanca, Dakar, Johannesburg, Lagos and Nairobi. For example, a recent UN-HABITAT report on the role of cities as engines of economic development stressed that while African cities contribute to 60 percent of the continent’s Gross Domestic Product (GDP), they account for only 34 percent of its population. There is, therefore, an urgent need to enhance the role of African cities as engines of economic growth and development, including through a better-targeted allocation of national budgetary resources to the development and management of cities and towns.

The main objective of the regional seminar was thus to urge African policy-makers to enhance resource allocation to key cities in their respective countries in order to accelerate national economic growth, generate greater employment and increase incomes.

Opening Remarks and Addresses

In his introductory remarks, Dr. Don Okpala, Chief of the Urban Economy and Finance Branch, and Acting Director of the Monitoring and Research Division of UN-HABITAT, welcomed participants to the meeting and stressed that the regional seminar was aimed to sensitize African policy-makers to the urgent need to enhance resource allocation to cities and towns throughout the continent as a means of strengthening their role as engines of economic development.

The opening address by Dr. Anna Tibajjuka, Executive Director of UN-HABITAT – delivered on her behalf by Mr. Daniel Biau, Acting Deputy Executive Director – stressed that the key to realizing Africa’s development goals firmly lies in unlocking the productivity- and growth-generating potential of cities. This, in turn, requires appropriate and adequate allocation of resources for

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5 The share is also increased by other (mainly urban-related) factors, such as industrialization, foreign capital inflows and increased trade. See R. Moonaw and A. Shatter, “Urbanization and economic development: A bias towards large cities”, Journal of Urban Economics, vol. 40 (July), pp. 13-37.
7 Ibid.
9 The full speech of Dr. Tibajjuka is contained in Part II of this report.
infrastructure development and basic services to enhance the development and management of urban areas.

In his welcoming remarks to the regional seminar, His Worship Dick Wathika, Mayor of Nairobi, congratulated UN-HABITAT for the initiative of convening the seminar and stressed the importance he attached to the greater allocation of financial resources by the Kenyan government to the development and management of Nairobi. He pointed out that Nairobi was a perfect example of how major cities function as engines of economic growth, as well as centres for production and consumption that contribute to a considerable share of national income and wealth creation. His Worship also noted that there was some discrepancy in figures representing Nairobi’s share of the national population and income, though part of the discrepancy is likely to be accounted by the disaggregation of the day-time and night-time population.

In his introductory presentation, entitled, “The role of cities in modern development: A view from Kenya”, Mr. Stephen Wainaina, Director of Economic Planning at the Kenyan Ministry of Planning and National Development, identified some of the major development challenges faced by African cities, including lack of integrated planning; urban sprawl and proliferation of illegal settlements; inadequate housing, water supply and sanitation; poor delivery of other basic services such as education, health and electricity; congested transport systems; lack of markets for small traders; growing insecurity and crime; and governance problems. The emerging policies required to deal with these and other problems included providing cities with either adequate resources or the means to raise such resources to fulfill their mandates; and reforms to help cities reduce the cost of doing business.

Finally, in a keynote address by the Kenyan Minister for Local Government – delivered on his behalf by Mr. Solomon Boit, Permanent Secretary in the Ministry of Local Government – His Excellency the Hon. Musikari Kombo emphasized that the development and management of urban areas requires partnerships between national governments, local authorities, development partners, and the private sector in order to mobilize adequate financial resources to meet the needs of modern cities and towns.10

Summary of Presentations

Enhancing Resource Allocation to Cities as Engines of Economic Development

Dr. Ananda Weliswita, UN-HABITAT, Nairobi, Kenya

This presentation drew upon the background paper entitled “Cities and the Wealth of Nations” (reproduced in Part II of this report) to identify the major challenges to enhancing the role of cities as levers of national economic growth and development.

The presentation highlighted the fact that while cities contribute significantly to the generation of economic output and employment opportunities in developing countries, the position of the city is still regarded as marginal in current debates on economic development strategies. International assistance to cities in developing countries remains modest in both scale and impact. For example, during the 1970-2000 period the total urban assistance to 11,000 cities in developing countries with two billion residents between them amounted to only about US$ 60 billion, or just US$1.00 per person per year.11

The presenter suggested that there is a contradiction between the scale and impact of urban assistance – notably for the provision of basic urban services – and the size of the global development challenge. At the same time, it was emphasized that assistance to cities must have broader and deeper economic justifications than simply providing basic services to the urban poor. The presentation then focused on several key justifications.

In the new globalizing world, cities are considered as centres of trade and financial markets. In a sense, all cities are being encouraged to become global cities, albeit at different scales. They are expected and encouraged to become the loci for open markets and the increased flows of goods and services. However, little is said about the risks cities and their constituents face in the process of globalization. The history of the 1990s has shown that cities face the brunt of sudden global economic changes,

10 The full speech of His Excellency the Hon. Musikari Kombo is contained in Part II of this report.

11 Unless otherwise stated, all figures mentioned in this presentation are derived from Prof. M. Cohen’s background paper contained in Part II of this report.
such as changes in relative prices, with capital and jobs arriving in good times and departing in bad times. The 1997 Asian currency crisis is a case in point.

One way to cushion cities and their economic activities and residents from sudden global economic shocks is to improve urban productivity, that is to say the productivity of urban-based economic activities. This increase in urban productivity can be financed by public and private savings, public and private expenditures, credit, public and private investment and other financial sources such as external aid and grants. Higher levels of urban incomes and productivity are the results of economies of scale and economies of aggregation, and cannot be fully attributed to the subsidized levels of public expenditures. Although public expenditures play an integral part in economic growth, the significance of internal markets and private capital flows cannot and should not be ignored. These other financial flows may be quantitatively much larger than public expenditures in some, though not all, developing countries.

Another way to improve the urban productivity is to implement urban economic policies that stimulate and sustain the economic multipliers needed to generate employment and incomes. While the traditional response to this question has been to finance urban infrastructure, it is apparent that infrastructure is a necessary but not a sufficient condition for continued economic activity. Local economic development strategies must be cross- or inter-sectoral, putting in place the incentives and conditions needed to create productive capacity and then finding ways to distribute and sell good and services.

The presenter then turned to major constraints to increasing the productivity of urban-based economic activities. One of the biggest constraints is the presence of infrastructure deficiencies, particularly in developing country cities. Evidence suggests that where water supply, electricity, transportation links and other services are not available, private sector enterprises spend up to a third of their gross fixed capital in providing these services for themselves. In other words, in the absence of adequate urban infrastructures, firms are taxing their profits for infrastructure, at the expense of their productive growth and thus the generation of new jobs. Infrastructure deficiencies thus contribute to hinder job creation, economic growth and the productivity of regions.

A second major constraint to improving urban productivity is unnecessary or inappropriate municipal regulation. Appropriate regulation is, of course, necessary to correct market failures and to ensure compliance with minimal labour, health and environmental standards. Economic regulation may be even more important in developing countries than in industrialized countries, because the risks of market failures in former tend to be much greater than in the latter. But in most cases, excessive and inappropriate regulation hurt private enterprises and, therefore, the entire economy. There are several reasons for this. First, unnecessary regulation increases both the cost of entry and the cost of doing business. Second, excessive regulation acts as an incentive for firms to remain small and informal. Third, inappropriate regulation can have heavy economic and financial costs that are rarely evaluated. In addition, excessive regulation is difficult to enforce, and encourages non-compliance and corruption.

Another constraint to improving urban productivity is poor governance of urban authorities. Technical and financial inefficiency of local urban authorities results in excessive delays and unnecessary costs to individuals and businesses. An important indicator of a well-functioning city is the quality of its governance and financial management. In fact, good governance and sound financial management are not only indicators of a well-functioning city, but they are also determinants of a well-run city.

A fourth constraint is the weakness of financial systems for local investment. The financial performance of cities depends, to a large degree, on the fiscal framework between municipal authorities and central governments. This fiscal framework determines how much tax a city can collect, how much of the tax revenue it can keep, and also the amount of central government transfers to municipal authorities. One of the reasons why the collection and management of local taxes are neglected in many countries is that they lack adequate fiscal decentralization. This tends to inhibit cities from being innovative in terms of revenue generation.

The presentation concluded by drawing attention to the fact that cities' ability to attract investments mainly depends on the efficiency of both the public and the private sector. Efficiency of the private sector and its ability to create more or better jobs and higher incomes is predicated upon adequate infrastructure, the depth
of economic multipliers, the size of domestic markets, appropriate economic policies, skilled human capital stock and good governance. Cities cannot and will not become engines of economic development in a vacuum. Cities' success requires deliberate national and local urban policies in support of their location, development and effective management.

In the ensuing debate, it was generally agreed that while cities have successfully taken on the role as engines of economic growth and development, this engine has not been functioning properly in the African context for a series of reasons.

It was stressed, for example, that national governments throughout the continent need to embrace the market approach and the business culture of incorporating innovative ideas in formulating policies and regulations. Several participants also pointed out that national governments in most African countries had embraced the policy of decentralization but in reality, physical and actual decentralization was not taking place due to technical problems, inefficiencies and inadequate human resources in local governments.

In addition, it was pointed out by several participants that urban-rural linkages should be reflected in government policies to promote sustainable growth and to maximize the benefits that arise from urban development. Furthermore, ineffective regulation and corruption has been an ongoing problem that needs to be tackled before urban economic growth can be enhanced in a sustainable and equitable manner. To that effect, national and local governments should also enlist active participation from the community by building awareness on the role of cities as engines of economic development.

It was further noted that African cities largely contribute to economic growth through value-added activities as they process primary commodities, such as coffee and tea coming from rural areas, into marketable products. This role of cities should thus be promoted and enhanced in order to increase productivity and social welfare. Many participants agreed that central governments should give urban authorities the means to cope with the increasing demand for local government services.

One participant suggested that the proportion of foreign direct investment flowing into China relative to the rest of the developing world shows that a strong government initiative in creating an enabling environment is necessary for attracting businesses to cities. It was also suggested that the regulatory environment in many African countries needed to be revised. Many countries are still using outdated pre-independence regulations that often create an inefficient and hostile business environment.

Finally, participants agreed that there is a fundamental data availability problem in many African cities: statistical data on key indicators are either not being collected properly or not being disseminated. The unavailability of reliable data underlies the inability to make accurate projections, and therefore, leads to inappropriate allocation of resources based on misinformation. Most participants further agreed that cities need to collect and disseminate accurate and updated data that monitors economic activity, using technology such as GIS in order to formulate appropriate responses at both urban and national levels. For example, poverty is increasingly becoming urbanized as information collected using GIS technology show more pockets of poverty in urban than rural areas. This fact is often ignored by governments which still formulate policies on the basis that poverty is mainly a rural phenomenon.
Mobilizing Public Finance for the Development of African Cities
Professor Aloysys Mosha, University of Botswana, Gaborone, Botswana

This presentation drew upon a background paper entitled “Mobilizing public finance for city development and management in African countries”\textsuperscript{12} to identify the major challenges to municipal finance in African cities.

The presentation drew attention to the fact that urbanization has become one of the most important trends in human settlement development, and the prospects of all developing countries continue to be deeply affected by rapid urban population growth, in not only Latin America and Asia but also, increasingly, in Africa. For example, while Africa was 80 percent rural in the 1950s and 1960s, its rate of urbanization now stands at 50 percent on average and the trend is expected to accelerate over the coming years.

The presenter suggested that a number of troublesome forces have accompanied the process of urbanization in Africa, including the fact that urban population and those moving to live in urban areas consist largely of unskilled labour. Secondly, municipal authorities have not been structured to cope with the fast-growing urban population; the existing revenue collection administration is generally inefficient and what is collected has, in some cases, been inappropriately managed. Thirdly, as municipalities are, in general, financially weak, they must rely on financial assistance from central government. Last but not least, the growing gap between available municipal revenues and the increasing expenditures associated with urban population growth means that many African cities are now faced with a financial governance crisis.

The presenter proposes a four-part agenda to tackle this increasing financial crisis in African cities: (i) municipal authorities should manage available resources more efficiently; (ii) they should also take the initiative to propose reforms in intergovernmental fiscal relationships, so that functional responsibilities can be clearly defined and revenue sources be expanded to meet required expenditures; (iii) new resources must be mobilized by municipalities, including responsible borrowing for investments in local services; and (iv) private participation

in the financing and delivery of public services should be actively promoted.

In the ensuing debate, it was generally agreed that African municipal authorities are not receiving adequate resources to fund required urban services, and also that more emphasis should be placed on building the capacity of local governments. Participants also agreed that municipal authorities should have a significant role in financing capital improvements and facilitating local investment through mechanisms available to them, including local revenue generated through tax and fee collection, public-private partnerships, equity sharing of capital projects, and borrowing from capital markets.

In addition, many participants noted that the private sector has an important role to play in enhancing urban productivity, and that governments should facilitate and build partnerships with the private sector in order to increase productivity and efficiency. It was further noted that companies cannot operate efficiently without basic services and infrastructure, and therefore governments should provide an enabling environment conducive to the growth and efficient operation of private enterprises. The debate concluded with a call for central governments to give municipal authorities the means to cope with the increasing demand for local services.

\textsuperscript{12} The full background paper is contained in Part II of this report.

Enhancing Resource Allocation to Urban Development in Africa
Mobilizing Private Sector Finance for the Development of African Cities
Mr. Wafula Nabutula, Nairobi Central Business District Association, Nairobi, Kenya

This presentation focused on private sector involvement in the provision of infrastructure and other essential urban services in developing countries. The presenter also emphasized that effective administrative decentralization is essential to enable cities to better manage service delivery by giving them the autonomy to set tariffs and user fees, determine the appropriate mix and level of services, and design efficient delivery methods, including involvement of the private sector.

The presenter pointed out, however, that urban low-income dwellers that are unable to pay economically-priced user fees should be assisted with carefully targeted subsidies. One way to target subsidies would be to identify specific households and provide them with vouchers to meet the costs of essential urban services. Another way would be to cover the costs of a minimum amount of consumption for all households, though that would also include higher-income groups.

The presentation then identified several options for private sector involvement and focused on their positive contribution to municipal finance and urban development. The four major options are as follows:

- Sub-contracting services can be beneficial, particularly when private firms compete to deliver urban services, since they are motivated to devise cost-saving technologies and improve efficiency in service delivery in order to reap the financial rewards for the results delivered;
- Corporatization should be implemented when governments need the technical expertise of the private sector to improve management, but also prefer to maintain overall responsibility;\(^\text{13}\)
- Leasing and concessions are recommended when a government is looking for the private sector to take on more financial responsibilities and risks. Usually, this means a longer-term commitment, from five to 10 years for leases, and 15 to 20 years for concessions;
- Full-scale privatization could be attempted when the market is well developed and the regulatory framework can ensure that fair pricing and adequate levels of coverage will be maintained.

The presentation concluded with an appraisal of the main challenges and opportunities for greater private sector involvement in service provision and municipal finance in eastern African countries. The speaker noted that rapid economic growth and urbanization had overwhelmed the region's already inadequate urban infrastructure, and stressed that the public sector alone cannot bear the burden of supplying, managing and maintaining this infrastructure and providing adequate services to meet the region's growing demand. Private capital, technology and management know-how are, therefore, urgently needed to accelerate urban economic development in the region.

The presenter recommended that coordination amongst East African economies and between export credit agencies of each economy be intensified in order to help finance infrastructure projects. It is also essential that a stable policy and macroeconomic environment be maintained and that foreign exchange convertibility be guaranteed. Finally, the presenter emphasized the importance of ensuring a competition-driven environment for private sector infrastructure projects and open non-discriminatory access to infrastructure.

The seminar participants agreed the private sector could bring much needed finance and investments for the expansion or improvement of urban infrastructure and services. However, it was also stressed that effective mechanisms must be in place to ensure that urban low-income groups are not priced out of the market through public-private partnerships or privatization of basic services. In addition, several participants suggested that greater private sector involvement be accompanied by an enabling strategy involving communities in the formulation and implementation of urban development policies, as well as campaigns to sensitize urban dwellers to the potential benefits of private sector participation.

\(^{13}\) Corporatization usually refers to the transfer of the provision of urban services from direct government control to state-owned enterprises, often run as private enterprises and by private-sector management.
Incentives to the Urban Informal Sector
Mr. Paul Okunlolade, The Guardian, Nigeria

The presentation started from the premise that urbanization, in the absence of concurrent economic growth, can be a major source of growing unemployment and social exclusion in African cities. Between 15 to 65 percent of African city dwellers are said to be living beneath the poverty line with little or no access to essential urban services, and employment in the informal sector is often the only escape route from chronic urban poverty that is available to unskilled migrants and other marginalized groups seeking jobs in the urban centers of most African countries.

According to the presenter, there are widely differing views on what should be the appropriate attitude and policy towards the informal sector. Some observers argue that the informal sector should be promoted for its roles in providing a vital source of employment and income for the poor, as the seedbed of local entrepreneurship, and as a potent instrument to combat poverty and exclusion. Critics, on the other hand, dismiss the sector as a source of disorder, tax evasion and an obstacle to the development of a modern economy.

In Nigeria, for example, the informal sector employs around 58 percent of the urban labour force and is comprised almost exclusively of small and medium enterprises (SMEs), which account for one-third of the country's GDP and as much as 90 percent of new job creation. Realizing the importance of the informal sector to economic development, the Nigerian Government launched a reform programme focused on addressing the barriers to small and medium enterprise development, namely (i) inadequate physical infrastructure; (ii) uncertain business environment; and (iii) insufficient access to finance.

A major aspect of the government's programme for tackling the problem of SME financing was the establishment of specialized Development Finance Institutions (DFIs), which provided capital to small businesses. This approach to SME financing has received mixed reviews. While generally applauding the government's active role and good intentions, the programme was criticized for being commercially unsustainable by key industry operatives.

Despite the potential of the informal sector to act as a catalyst for stimulating economic growth, the presentation identified several challenges which limit its ability to achieve this function. These include (i) weak and sometimes non-existent regulatory mechanisms; (ii) low productivity and incomes; and (iii) low level of investment, among others. Furthermore, the development of the urban informal sector often depends on access to funding, land, and security of tenure; the provision of basic infrastructure and services; the harmonization of local authority charges; and economic stability and consistency in government policy.

In the ensuing debate, participants agreed on the following points:

- The informal sector is a fact of life in all major African cities and governments therefore need to understand the characteristics of the informal sector to find an appropriate mix of policy interventions;
- The growth of the informal sector is mainly driven by prohibitive entry barriers into the formal economy and by rural-to-urban migration of unskilled labour. As such, governments should examine ways to lower the entry barrier, implement training and retraining programmes for urban migrants and provide easier access to finance and information;
- Governments should examine institutional weaknesses that lead to the growth of the informal sector, and harness the informal sector's potential to contribute to the development of cities by considering innovative approaches to informal sector challenges.
Recommendations of the Seminar

As stressed at the beginning of the report, the main recommendations of the seminar are ultimately aimed at promoting awareness among African decision- and policy-makers of the need to enhance resource allocation to key African cities as a means to generating greater employment opportunities, increasing urban incomes and thus accelerating urban and nationwide economic and social development.

The seminar reiterated the major economic benefits of cities, notably their provision of economies of scale and agglomeration for the acceleration of national economic growth. While cities can play a key role in national economic development, efforts should also be made to strengthen urban-rural linkages within a territorially balanced development strategy that also allocates resources to secondary cities and towns.

Participants also agreed, however, that cities as engines of economic growth are not working well in Africa for several reasons:

(i) There is a growing gap between the demand for the delivery of municipal services (and associated capital expenditures) to growing urban populations on the one hand and the financial resources available to municipal authorities to fund those services;

(ii) Blame cannot be placed only on decreasing (or fluctuating) central government transfers to cities, or on central government control of high-yielding taxes, but also on local factors, such as poor financial management, lack of local institutional and managerial capacity, inability to collect local taxes efficiently, etc.

(iii) There are several other important constraints associated with lack of enabling environment for local economic growth, such as infrastructure deficiencies, unnecessary/top-heavy regulation, inadequate local financial system and poor governance.

The potential solutions and policy options recommended by the seminar are divided into three categories: (a) those in the area of public finance; (b) those directed at private finance; and (c) policies in other key areas.

(a) Public Finance

- Central government provision of physical infrastructure; human resources, managerial and regulatory capacities to enable municipal authorities to generate greater income and to recover greater share of costs;
- Enhancement of local tax collection capabilities;
- Fiscal decentralization;
- More predictable central government transfers, to allow municipalities to plan capital expenditures over the medium to long run;
- Greater cost recovery of user charges that also incorporate social considerations and the interests of lower-income urban dwellers (e.g., free delivery of minimum amounts for basic human needs, and progressive charges beyond that minimum amount);
- Greater use of municipal borrowing arising from enhanced financial governance and local creditworthiness, as well as government/institutional credit guarantees to create an enabling environment for more successful municipal borrowing;
- Good governance and improved urban management practices, including better accounting practices, more efficient use of resources, innovative municipal financing tools, better administrative structures, better accountability, and recognition of social-cultural aspects;
- Greater use of (tested/successful) good practices that can be tailored to local (African) conditions.

(b) Private Finance

- The private sector can bring much-needed finance and capital expenditures (to complement scarce public funds) for the expansion or improvement of urban infrastructure; as well as efficiency improvements, technical and managerial skills, better service delivery and greater cost recovery;
- Mechanisms must be in place to ensure that low-income groups are not priced out of the market through strategic public-private partnerships (PPPs), with clearly specified roles for the public and private sectors,
clear identification of risks and benefits, cost sharing and effective regulation/supervision by governments;
- Enabling strategies involving communities in formulation/planning and implementation stages, as well as campaigns to sensitize urban dwellers to the potential benefits of private sector participation, together with the availability of safeguards that can be put in place.

(c) Other Key Issues

- Policies to benefit from the development of the informal sector in terms of its contribution to employment generation, wealth creation, municipal revenue generation and urban socio-economic growth;
- Particular attention and recognition should be given to the central role played by women in the urban informal sector in most developing country cities;
- The informal sector is a necessary tool to support the development of the formal sector, bearing in mind the existence of hindrances and loopholes;
- Streamline municipal regulation to support the development of the informal sector and gradual steps to formalize it;
- Mobilization of "hidden" community resources - a participatory approach to economic development - including greater participation by NGOs and community associations in urban planning and management;
- Provision of adequate data for accounting and financing of urban development.
PART II. OPENING ADDRESSES AND BACKGROUND PAPERS

Opening Address by Dr. (Mrs.) Anna Kajumulo Tibaijuka, United Nations Under Secretary-General and Executive Director of UN-HABITAT
[Delivered by Mr Daniel Biaw, Acting Deputy Executive Director, UN-HABITAT]

Your Worship Mayor of Nairobi,
Ladies and Gentlemen,

On behalf of the United Nations Human Settlements Programme, it gives me great pleasure to welcome you to this Regional Seminar on “Enhancing resource allocation to cities to strengthen their role as engines of economic growth and development”.

As you may recall, the theme of last year’s World Habitat Day was Cities – Engines of Rural Development. Last year’s conference on urban-rural linkages leading up to the World Habitat Day celebrations and this regional seminar are part of UN-HABITAT’s ongoing efforts to promote sustainable and territorially balanced economic growth and social development.

The role of cities as engines of economic development has gradually moved to the forefront of the international development agenda, and we strongly believe that cities are engines not only for rural development, but also for overall national economic and social development.

The process of urbanization and the growth of cities have, in many countries, been the basis of national development. Cities attract investment and create wealth by serving as centres for production and consumption, technological innovation and specialized services. Cities enhance social development and harness human and technical resources, resulting in unprecedented gains in productivity and competitiveness. This is most evident in the lion’s share of national income generated by many cities in developed and developing countries, including here in Africa.

You will see in the background report for this meeting, entitled, “Cities – Engines of Economic Development”, that cities in Africa contribute about 60 percent of the continent’s GDP, yet they only accommodate about 34 percent of the continent’s population. For example, while Nairobi is host to eight percent of Kenya’s population, its share of GNP is more than 20 percent. Similar trends can be found in several large African cities, such as Addis Ababa, Cairo, Cape Town, Casablanca, Dakar, Johannesburg and Lagos.

It is, therefore, clear that the potential for realizing the Millennium Development Goals lies in unlocking the productivity and growth-generating potential of Africa’s cities and towns. This, in turn, requires appropriate and adequate allocation of resources for the development of urban infrastructure and services. Since cities throughout the world can be powerful instruments for national economic and social development, it is also increasingly recognized that they deserve the support of deliberate national policies and enabling legislation.

Despite ample evidence supporting the correlation between the level of urbanization, GDP growth and per capita income, national budget allocations, particularly in Africa, have often failed to provide adequate resources to stimulate the economic growth and contribution of cities. For example, Lagos accounts for 11.5 percent of the Nigerian population, produces about 70 percent of value-added in manufacturing, hosts 65 percent of the country’s commercial establishments, and yet receives only about 2.6 percent of national fiscal allocations, 6.7 percent of national VAT allocations, and just 3.6 percent of municipal transfers. The emphasis that many African governments continue to place on rural development has also led the donor community to favour the rural sector, giving little scope for urban development and overlooking the significance of the mutual dependence between urban and rural areas.
Ladies and gentlemen, it is vital that there be increased awareness of the contribution of cities to national economic growth and poverty reduction, and much more focus on how better to allocate national financial resources to the development and management of cities and towns. It is also important, of course, that cities mobilize their own financial resources through proper fiscal policies, including, in particular, a better use of land and property taxation.

It is, therefore, my sincere hope that this regional seminar will:

(i) Provide a forum for sharing regional experiences and stimulate mutual learning and capacity-building, as well as sensitizing both national and local-level decision-makers to the importance of allocating greater resources to strengthen the role of cities as engines of economic development; and

(ii) Identify policy incentives and arguments that could be advanced to persuade governments to enhance budgetary and human resource allocations to cities and urban development.

I am confident that sharing our knowledge and experiences, as policy analysts and policy-makers in the relevant ministries and departments of your respective national governments, will be invaluable towards achieving our objective of promoting enhanced resource allocation to African cities, and ultimately result in accelerating national economic growth and development, generating greater employment, increasing incomes, and combating poverty.

This is the beginning of a series of such seminars which we hope to take to sub-regional levels. I very much look forward to the outcome of this seminar and to getting the benefits of your experience.

Thank you for your kind attention.

Keynote Address by Hon. Musikari Kombo, Minister For Local Government, Kenya
[Delivered by Mr. Solomon S. Bait, Permanent Secretary, Ministry of Local Government, Kenya]

Mr. Chairman,
Distinguished Guests and Participants,
Ladies and Gentlemen.

It gives me great pleasure to be invited to speak at this important regional seminar on enhancing resource allocation to strengthen cities and towns in Africa. In the past, African countries have not recognized and adequately supported cities and towns as engines of economic growth and development of the continent.

I am sure you are aware from experience and literature that African countries have focused their resources more on rural development in the last 40 years. However, these rural areas have become more urbanized with villages becoming towns, towns becoming cities, and cities becoming mega-cities. The African continent had been the more rural but is now the one urbanizing fastest. This rapid urbanization in Africa has created problems of governance and service delivery, including proliferation of slum and squatter settlements, environmental degradation, poor infrastructure and social services, inadequate income and employment opportunities, and increasing insecurity, among others.

Due to the above problems, cities and towns in Africa are now increasingly being recognized as important engines of economic and social development. However, this development requires partnerships between national governments, local authorities, development partners and the private sector in order to mobilize adequate financial resources to meet the needs of modern cities and towns. As engines of development, cities also need to be well planned, and serviced with both physical infrastructure and basic services. In this way, cities will positively contribute to both rural and urban development. Sustainable urbanization will require food security to be guaranteed by the agricultural sector in rural areas.

Although 70 percent of the population in African economies live in rural areas, current rapid urbanization is soon transforming these countries into urban status.
In the next two to three decades, urbanization is going to be accompanied by rapid changes in technology and lifestyles. The cities and towns of Africa will need adequate financial resources to manage this transformation to ensure sustainability.

In most African countries, a large share of national budgets is allocated to rural development programmes. This has been based on the argument that a majority of the population live in rural areas. As a result, less money has been allocated to management and development of cities, towns and other urban centres. This is irrespective of the fact that more resources are required to ensure sustainable development in the face of rapid urbanization in the continent.

Ladies and gentlemen, lack of adequate resources, in terms of finance, equipment and human resources has left local authorities who run these cities and towns with heavy debt. Their capacity for development and management of infrastructure is compromised. Financial management is unsatisfactory, as it is not in accordance with accepted international financial management standards. The revenue base is poor. The majority of local authorities are unable to collect local revenues, e.g., rates, licenses, fees and charges. Their budgets do not balance, hence indebtedness leads to poor service delivery. Most of these urban local authorities are not able to hire and retain adequate and well qualified, experienced human resources. They are not able to pay qualified human resources from central government or the private sector.

In a number of cases, the institutional and legal arrangements for local authorities who manage these cities and towns are not appropriate or enabling. Some are archaic or obsolete. Most local authorities also have no adequate autonomy to raise revenues and manage their affairs. These local authorities do not receive adequate resource transfers from central government.

Few African countries have institutionalized appropriate fiscal transfers from central to local government for service delivery. In Kenya, the government has established a number of fiscal transfers which benefit cities and towns. A Local Authority Transfer Fund (LATT), which was established in 1999, allocates five percent of total national income tax revenues which are distributed to all local authorities for service delivery and debt repayment. This fund is based on agreed criteria which include population size. This particular criteria, by coincidence, helps to allocate more of these funds to cities and towns. The Kenyan government has also established constituency development funds distributed to all constituencies. These funds also help to finance programme in cities and towns through resources allocated to urban-based constituencies. The Kenyan government is also allocating funds from the fuel levy fund, which is a tax levied per litre on fuel consumption in the country for road maintenance. The funds from the levy are distributed by the Kenya Roads Board for rehabilitation and construction of road programmes in local authorities through the Ministry of Local Government.

The development of cities, towns and other urban centres requires partnerships in resource mobilization between central government, local authorities, the private sector, development partners and residents.

Until recently, most development partners have targeted their resources towards rural or agricultural development, and neglected urban development. This is because towns have been viewed not as engines of economic development, but as parasites to the rural and agricultural sector. They have also been viewed by sociologists as taking away resources, especially the best human resources, from the rural agricultural sector, thus impoverishing rural areas.

This view disregards the interdependency between urban and rural development in Africa. African governments now need to integrate the rural and urban sectors in development planning, taking into consideration the strength, weakness, opportunities and threats of each sector. Integrated planning and development will ensure that cities and towns do not become centres for the underdevelopment of rural areas.

Most African countries have not formulated urban development policies to guide urban development in this millennium. Very few local authorities in Africa have the strategic corporate or development plans that would facilitate orderly development and management of cities, towns and other urban centres. In many of those that have such plans, these are obsolete.

Considering the importance of cities and towns as engines of economic development, it is my request that African countries, with support from UN-HABITAT, raise the issue of African cities and towns on the agendas of the African Union, the UN and other international fora.
The issue should also be raised at the African ministerial conference on housing and urban development, which was first held in Durban, South Africa last year to deal with urban and housing problems on the continent. The issue of cities and towns should also be placed on the agenda of the NEPAD cities programme. The role of professionals in Africa in enhancing development of our cities and towns is yet to be felt. The professional associations need to be proactive on issues concerned with cities and towns in Africa. Deliberate actions need to be put in place by African governments to involve the private sector in Africa in the development and management of African cities and towns as engines of economic growth and development.

My ministry, which is responsible for urban development in Kenya, is taking the necessary steps to formulate urban development policies to deal with the rapid urbanization of this country. I have also directed all local authorities to prepare strategic corporate and development plans to guide urban development in Kenya. Already teams in the ministry are working out on the necessary guidelines and modalities.

Finally, it is my great hope that this seminar will empower all participants with the tools to mobilize resources for the planning and development of our cities and towns. It is also my hope that you will be agents of advocacy for the urban development agenda in national budgets, and development plans and programmes in your countries. I also wish to appeal to our development partners to support the orderly development of our cities and towns as engines of economic growth and development in Africa.

Ladies and gentlemen, with these remarks, may I declare this seminar officially opened.

Thank you.

Cities and the Wealth of Nations
Prof. Michael A. Cohen, New School University, New York, USA

1. Introduction

Despite the growing importance of cities in national economies, demographic profiles, global and national cultures, and political life, the position of the city is regarded as marginal to current debates and development controversies. International assistance to cities remains modest in scale and impact. Total urban assistance to developing countries from 1970 to 2000 amounted to about US$60 billion, or US$2.0 billion per year. These resources were divided into projects and sub-projects affecting some 11,000 cities and towns in the developing world.\(^{14}\) While these numbers appear, at first glance, to be large, they are small in relation to the two billion urban dwellers in developing countries, each with about US$30.00 average annual income. Indeed, the modest amount of international assistance to cities is reflected in the contrast between global projections and the Millennium Goals endorsed by heads of state at the United Nations in 2000.

While some two billion additional urban dwellers are expected in the cities of developing countries by 2025,\(^{15}\) the Millennium goal is to improve the living conditions of 100 million urban slum dwellers by 2020, or a modest five percent of the total new demand for urban services.\(^{16}\) Phrased differently, even with the concerted effort announced by the Cities Alliance – a consortium of multilateral and bilateral international aid organizations providing basic urban services at a larger scale – over the last few years, it is highly likely that more people will lack services by the end of this period than do at present. This is analogous to the contradiction of the International Drinking Water and Sanitation Decade of the 1980s: at the end of the 1980s, more people had no water than at the beginning, even though 550 million people received water during this period. Was the Water Decade a failure? Not

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14 Author's estimates based on OECD DAC data.
for the households receiving water; yet the programmatic goal of “solving the problem” or “making a dent in the problem” was not reached.

Another approach to this problem has focused on building the capacity of international, national, and local institutions to manage cities and provide needed services. Over the past decade – from the height of preparations for the Habitat II Conference in Istanbul to the present – there have been myriad conferences and initiatives in the name of capacity building, i.e., teaching people to fish rather than giving them fish. Yet analysis of capacity-building efforts within the urban assistance programmes of multilateral and bilateral aid institutions suggests that, rhetoric aside, most of these institutions have actually not devoted more than 10 percent of their aid towards this objective. This is disappointing, but is also a significant indicator of the priorities and modalities of these institutions as they approach cities. The argument that the costs of training programmes are small in comparison to infrastructure does not explain away this low priority. If training is not expensive, one might ask, why not do more? The fundamental similarity between the programmes of the respective donor agencies leads to the conclusion that “if your only tool is a hammer, every problem is a nail.”

This contradiction, between the scale and impact of assistance and the size of the global development challenge to be addressed, suggests that assistance to cities must have other, broader, and deeper justifications than simply providing basic services to slum dwellers. The “place” or priority of cities and towns in national economic and social development strategies must be reframed, with new justifications and importance. Finding these justifications requires reframing the question, a process with which proponents of urban assistance have had long experience.  

During the 1970s, urban assistance began as support for low-cost housing solutions accompanied by basic infrastructure – sites and services and slum upgrading. Aid agencies in effect entered the city “through the house and the bathroom”. In the 1980s, a new emphasis was added: a shift towards strengthening the capacity of local institutions, primarily municipalities, as assistance was provided to improve “urban management”. In the 1990s, new emphases went in two directions: first, on enhancing the contribution of cities to national economic and social development and, later, on encouraging the development and efficient functioning of markets. An assessment of current aid policy documents and Websites suggests that present emphases seem to be rooted in the Millennium Goals and City Development Strategies as proposed by the Cities Alliance. The narrowing of objectives may be useful in political and institutional terms for the various institutions of the international aid community. However, this narrowing may actually have the effect of cutting off a needed, wider debate about how strategies for helping cities can be developed without accepting such contradictions as the objective of the Millennium Goals addressing only five percent of the problem.

Given the history of shifting justifications and very different views of the meaning of “urban”, even by the same institutions and professionals, this paper poses the question: what are the broader justifications for urban assistance within contemporary, evolving global debates about macro-economic and development strategies? Indeed, how are urban phenomena related to the most challenging and controversial debates of the day?

2. The City and the Neo-Liberal Framework

The current heated debate between developing countries and the institutions defending the “post”-Washington Consensus – the IMF, the World Bank, the WTO, and many donors – suggests profoundly differing views of the world at this time. The marginal changes between the old and the new “orthodoxy” are disappointing to policy-makers, politicians, activists and analysts in many developing countries. The persistent emphasis of the ‘post-Washington Consensus’ on “outward orientation” seems to place countries at continuing risk in the face of the

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volatility of world markets. In this scenario, the city is an “entrepreneur” for trade and a centre for the financial markets. In a sense, all cities are being encouraged to aspire to becoming “global cities” in Saskia Sassen’s terms, albeit at different scales. They should be the loci for opened markets and flows of goods and services of all kinds. Yet in this scenario, little is said about the risks to cities and their populations. The history of the 1990s has shown that cities also bear the brunt of sudden global economic changes, such as relative prices change, with capital and jobs arriving in good times and departing in bad.

This policy position is contradictory, because international institutions recognize, at least on paper, that cities generate more than half of GDP in all developing countries, and up to 80 percent in the more urbanized countries of Latin America. This would logically suggest that the economic futures of countries are closely tied to urban physical and spatial environments. Yet there is little apparent institutional intention to protect or cushion cities from external shocks. This policy orientation, moreover, also ignores the city as the site where the economic multipliers of internal domestic markets operate. It is more than 30 years after the publication of Michael Lipton’s influential book, Why the Poor Stay Poor: Urban Bias in Developing Countries. Yet some policy analysts are still trying to justify creating “level playing fields” and shifting rural-urban terms of trade toward rural production by reducing urban subsidies in the name of equity and productivity. This policy objective might have had some validity 30 years ago, but is hardly defensible today, unless nostalgia is a justifiable criterion for national economic development policies.

Indeed, in historical terms, the productivity of urban economic activities is more important than ever before. This productivity is financed by public and private savings, public and private expenditures, credit, and public and private investment. Higher levels of urban incomes and productivity are the results of economies of scale and of location and cannot be attributed to subsidized levels of public expenditure. Those who believe that public expenditures are the critical factors in economic growth fail to understand the significance of internal markets. Other financial flows may be quantitatively much larger than public expenditures in some, although not all developing countries. In most cities, most financial transactions originate in the private sector. For example, in no country other than China has more than 15 percent of the housing stock been financed by public funds. Public expenditures can be important as catalysts for other flows, i.e. they can “crowd in” private investment. Cities in which private financial stimulants for economic activity are constrained will also find that economic multipliers dry up – as occurred in Buenos Aires during the crisis in 2002-2003.

This warning implies that cities require what might be termed “Neo-Keynesian policies”, i.e. expansionary economic policies which stimulate and sustain urban demand and hence the creation of urban employment and generation of incomes. Both public and private expenditures have important roles to play in this process. Sustaining continued economic expansion is even more important due to continued urban demographic growth. This advice is well understood in the North – indeed all governments in Europe and North America follow this policy direction, regardless of which party is in power. Yet, as Joseph Stiglitz points out, the IMF offers the opposite advice to countries of the South, through repeated insistence on restraining public expenditures to manage the fiscal deficit as the key indicator of macro-economic performance.

The issue for the debate on urban policy, therefore, is how to support urban economic policies to stimulate and sustain the economic multipliers needed to generate employment and incomes. While a traditional response to this question has been to finance urban infrastructure, it is apparent that infrastructure is a necessary but not a sufficient condition for continued economic activity. Local economic development strategies must be cross-sectoral, putting in place the incentives and conditions needed to create productive capacity and then finding ways to distribute and sell goods and services. Urban economic development should not be understood

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23 Michael Lipton, Why the Poor Stay Poor: Urban Bias in Developing Countries; (Cambridge: Harvard University Press, 1974).
solely as investment, which is frequently the case, but rather as active continuous engagement in building and reinforcing linkages and markets. These linkages and markets should also be built with space and location in mind, utilizing density as an important condition for supporting economic and social interaction. Jane Jacobs developed similar arguments in her book, *The Nature of Economies.* Going a step further, supporting interaction also requires reducing obstacles and constraints, for example, unnecessarily heavy and costly regulatory frameworks, such as the classic example of the 55 steps required to obtain a building permit in Kuala Lumpur.27

3. Economic Globalization and the Role of Cities

When we discuss these issues, we must remember that the economic history of the world during the 20th century has dramatically demonstrated that the processes of urbanization and economic progress are mutually reinforcing.28 The explosion of political and economic development in Africa, Asia, and Latin America in the post-World War II period fueled and was fueled by the movements of peoples, knowledge, technology, and wealth. As in earlier periods, much of this activity involved movement to cities and towns or was itself based in urban areas.29 The experiences of developing countries in all regions indicate that urbanization is closely associated with increasing levels of income and improvements in social indicators such as life expectancy, literacy, infant mortality, and access to infrastructure and social services.30 Countries that urbanized earlier than others have higher incomes, more stable economies, stronger institutions, and are able better to withstand the volatility of the global economy.31 A study of 90 countries from 1960 to 1980 concluded that the urban share of population itself increases with national income per capita; the share is also increased by industrialization, trade orientation, and foreign capital inflows.32

Aggregate data are supported by numerous country studies which show the important role of individual cities in their national accounts. These data and many supporting studies conclude: "cities, especially bigger cities, mean higher productivity and higher per capita incomes. The results...remain consistent for nations with different economic systems...and cannot be simply explained by what some would call the unequal development patterns of (capitalist) free market economies."33 In the 21st century, regardless of ideology, cities are the loci and motors of economic and social change.34

Yet, despite this evidence, it is surprising that urban growth and the urban share of the national economy, either as GDP or as locus of production, trade, and exchange, is rarely recognized in global debates about economic and development policy. It has been known for more than a decade that urban-based economic activities account for more than 50 percent of GDP in all countries, and up to 80 percent in more urbanized countries in Latin America, or more in Europe.35 The 10 largest metropolitan areas in Mexico, accounting for a third of the country’s population, generate 62 percent of national value-added.36 This disproportionate economic contribution of cities, indeed their importance to the economy as a whole, is normally ignored or, more politely, overlooked. This neglect is dangerous because, as this paper will show, cities and towns are not only the loci of production, but they are also the loci of the most important impacts of globalization and hence, the spaces of change and for building the future. Undervaluing urban areas can unwittingly place the economic and social futures of countries at risk. Improving our understanding of the multiple interactions between globalization and cities can therefore contribute

36 *Cities Transformed,* p.303.
to identifying new strategies for protecting and sustaining urban economies, and hence national economies, over the longer term.

4. Global Economic Dynamics

The transformation of the global economy in the last two decades is perhaps the most important dimension of globalization, because it has supported the diffusion of global culture and provoked deep and broad adjustments within countries and cities. Flows of capital, labor, technology, and information have supported the growth of world trade from $579 billion in 1980 to $6.272 trillion in 2004, an increase of 11 times. Trade itself has become an increasing share of the GDPs of national economies, going from 3 percent in 1980 to 20 percent in 2004. What began as trade in goods and services is now accompanied by the flow of capital and the exchange of currencies in world financial markets which themselves are equal, on a daily basis, to the GDPs of many countries, more than all of Africa and Latin America combined. Information technology has allowed the birth of global interest rates and the increasing movement of capital to new opportunities for immediate and short-term financial benefits. Concerns about “footloose industries” have given way to cyber-markets for finance and investment. Events in East Asia are not only immediately felt in interest rates in Bangkok, but they change investment decisions in Barcelona, Boston, Brisbane, and Buenos Aires. Investors and financial managers felt the impacts of the Tequila effect in 1994-1995, the Asian crisis in 1997, the Vodka effect in 1998, the Samba effect in 1999, and the Tango effect in 2001-2002.

Since the mid-1990s, these changes have been amplified by processes of trade and financial liberalization. Governments and multi-lateral institutions believed that “open markets” would attract investment and foster growth. While these policy changes have benefited some countries, others have been unable to cope with the pace and scale of change. In particular, developing countries with shallow financial markets, non-diversified exports, and labour-intensive industries were unable to compete with more endowed and/or developed countries. Inequality of incomes between countries grew over this period, leading to the judgment by many economists that “the fruits of globalization” were not equally enjoyed.

The differences in attractiveness to investors between countries is reflected in the great concentration of foreign direct investment in a set of 10 countries (China, Brazil, Mexico, Indonesia, Thailand, etc.) and the almost total exclusion of others, largely the poorest countries and mostly those in Africa. This distribution of the “fruits of globalization” reflects private sector judgments about the expected financial returns to these investments, their security, and the economic and political environments in which they occur.

At the city level, the rapid entry of new, mostly foreign, investors and new capital led to changes in the composition of economic activity, particularly favoring financial services and those industries able to benefit from connectivity. The role of “global cities” and global circuits of networked cities, both identified by Saskia Sassen, led to “new geographies of centers and margins”. These spatial impacts will be discussed below, but they are also reflected in the change in the composition of urban employment and value added during the 1990s. Buenos Aires, for example, saw more than 50 percent of its employment switch sectors, as many medium-sized enterprises closed in a process of de-industrialization, including more than 4,600 enterprises from 1995 to 2,000, or about two per day.

Two major changes in the composition of employment occurred in many cities in both developed and developing countries over the last two decades. First, there have been greater financial returns to jobs in the financial sectors and those activities involved in access and management.

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38 Ibid.

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Enhancing Resource Allocation to Urban Development in Africa
of information. These jobs, many requiring university-level education, have been part of the emerging pattern of interconnected global financial markets. At the national and local levels, they include international banks, insurance companies, and a wide range of financial services previously not accessible to most urban residents around the world. They are knowledge-intensive industries in which technology and connectivity determine profitability and employment profiles.

At the same time, capital has been attracted by the high returns to these sectors and away from industrial production. The lowering of trade barriers in many countries, coupled with improved transportation networks and multi-national production processes for many manufactured goods, has meant that differentials in wage costs have become more important in the global competition among products. This has in turn meant the flight of capital and jobs to locations with lower wage costs. This process has been evident in many previously productive urban industrial cities in the United States, such as Detroit, Chicago, New York, and San Francisco, which have lost large shares of their employment base as companies have moved to other countries, seeking lower wages and fewer labor and environmental regulations. Even many maquiladora enterprises of Northern Mexico have closed as their owners have moved their businesses to China in search of lower costs and higher profits. This process has been referred to as “the race to the bottom” and it challenges many of the asserted wage benefits of trade liberalization. There is strong evidence, for example, that female wage levels and working conditions have dropped in many countries in East Asia as a result of the dropping of barriers to footloose industries. Studies in other regions document similar processes.

The “race to the bottom” also occurs at home, resulting in job loss where large segments of the labor force have to shift from one sector to another, often losing jobs with benefits and job security while having to compete for income-generating opportunities without such benefits. This leaves many people unable to obtain stable jobs and incomes and thus unable to afford housing and other essential services. The consequential patterns of social exclusion vary across cities, but they often are reflected in other social cleavages as well, such as along racial and ethnic lines.

This in turn accelerates and increases the process of “informalization” of the urban economy, with increasing shares of incomes earned in non-formally regulated employment. Several economic processes converge to “informalize” employment and other aspects of urban life. The closing of formal sector enterprises often coincides with the downsizing of ancillary industries and services having further multiplier effects in urban areas. For example, declines in one industry, light engineering, in Karachi led to reduction in incomes in the city as a whole. Former employees were no longer able to purchase so many services on the street; hence, street vendors also suffered. Simultaneously, if utility tariffs increase, as they did in Karachi in the 1990s, other enterprises suffer and are forced to reduce their operations or close altogether.

The twin processes of informalization and de-industrialization demonstrate how competition intensifies between and within urban labor markets. In a policy environment of few barriers to financial flows and investment, there is little to arrest the continued shifting of industrial investment and employment to sites of lower wages. The example of “outsourcing” of major commercial functions from accounting, to medical analysis, to telephone calls from the United States to India illustrates how the mobility of resources both connects and disrupts the economic lives of cities.

5. Productivity

Let me turn now to the issue of productivity. We know that since the mid-1980s, more than half of GDP in all countries comes from urban-based economic activities. At the same time, we see increasing levels of poverty in cities,
certainly in poor countries, and even in rich countries. Indeed, one of the great paradoxes of cities in both rich and poor countries is, why are cities not more productive than they already are? What are the constraints to the productivity of urban-based economic activities?

In 1991, I wrote an urban policy paper for the World Bank which identified four major constraints to urban productivity. I want to mention them because I believe they are relevant to our debate.

5.1 Infrastructure Deficiencies

The first constraint is infrastructure deficiencies. Let me suggest three examples to illustrate this point:

(i) In the late 1980s, a research project was undertaken by a Korean researcher, Kyu Sik Lee, and his colleagues to estimate the economic impact of infrastructure deficiencies in Nigerian cities. He surveyed more than 200 small and medium-sized firms and discovered that when water supply, electric power, transport, solid waste removal, and other services were not available, companies invested up to 35 percent of their gross fixed capital in providing these services for themselves. Studies of this kind were also undertaken in Jakarta and Bangkok, where more infrastructure was available, but the response of firms was similar. In effect, this means that firms were taxing their profits for infrastructure and placing upon themselves very heavy constraints to their growth and in the generation of new jobs. Infrastructure deficiencies in effect limit job creation, economic growth, and the productivity of regions.

(ii) A second problem demonstrates that this experience is not just limited to developing countries. During the 1990s, Chicago and New York experienced repeated infrastructure failures, including breakage of water supply systems and electricity blackouts, including the recent one in August 2003 in the northeast of the United States. These failures produced enormous economic losses. In fact the 9/11 attacks themselves meant that New York City lost $110 billion in infrastructure, buildings, jobs, and other economic losses. This scale of loss is equivalent to wiping Portugal from the map for one year.52

(iii) The third dimension of this issue is demonstrated by two studies produced in the 1990s: the World Bank's World Development Report of 1994, focused on infrastructure,53 and a 1993 study of US infrastructure by the US National Academy of Sciences.54 Both studies concluded that most infrastructure projects are too big, too expensive, and involve capacity to provide services which frequently are not needed. In fact, infrastructure projects often reflect a large "supply bias", i.e., they reflect the design preferences of the engineers who build them, but such projects frequently are unconnected to the demand side or the potential users of these services. It should be no surprise that these projects frequently create services which the public utilities cannot sell. As a result, infrastructure projects frequently place local authorities in financial difficulties.

Taken together, these examples suggest that a necessary priority for local and regional institutions is to assure the efficient functioning of infrastructure.

5.2 Regulation

A second constraint on the productivity of cities is unnecessary regulation. I do not mean to argue that all regulation is bad, because that obviously is not the case. We can easily see the importance of regulations affecting the environment, health, and conflicting land use as examples of good regulation. But in working on cities in many countries, I have encountered some cases which make me wonder about the general situation of regulation in other cities. For example, my former colleagues at the World Bank found that there were 55 steps required to obtain a building permit in Kuala Lumpur, Malaysia. This process took three years and through the delays, added costs equivalent to three percent of Malaysia's GDP. In South Africa under the apartheid regime, there were 27 steps. Now they have been reduced to nine, but it raises a set of interesting questions about the value of regulation.
and its impact on economic and social activity in the city. Am I correct in assuming that obtaining permits is very easy in Spain? If we are interested in improving the efficiency of our cities, how do such regulations affect the pace and cost of economic activity? One tool to answer such a question would be to undertake a regulatory audit — an evaluation of all the rules which exist for a specific sector, asking the question, what is the value-added of the regulation?

A recent World Bank report cites the economic cost of inappropriate regulation. It is interesting to note, however, that Nobel Laureate Stiglitz argues that more regulation may be needed in developing countries where the probability of market failures is higher than in developed countries. Stiglitz, therefore, argues for more regulation, if it is targeted to address these market failures. Of greatest concern here are the negative social and economic impacts on the poor who most frequently feel the impacts of market failures in the cities, for example, paying higher prices for water or food than the rich. This issue needs to be taken quite seriously, because it has direct consequences for the quality of urban life.

5.3 Local Government

A third constraint to productivity is the technical and financial efficiency of local government. I remember my relationship with the Municipality in Washington, D.C. One year I received a water bill for $20,000 for one month for my house. It took a year to resolve the issue. I had a modest house in downtown Washington and certainly did not have a swimming pool. Or each time I had to renew my driver's license, I lost a day of work. If the customer/citizen side of the municipality was slow and bureaucratic, I can only imagine how slowly other activities worked. Working in Chennai (Madras), India, I found that there were 2,000 false employees working for the municipality. Many had been dead for 20 years, but someone was collecting their salaries. Taxpayers were paying multiple salaries to individuals.

If, in some cases, the issue is corruption, in other municipalities there is simply a lack of technical and financial capacity to do what needs to be done. In many developing countries, the "best and the brightest" municipal personnel transfer to national governments or the private sector to advance their careers. In other cities, the absolute lack of financial resources means that maintenance is constantly deferred. This has a heavy impact on the infrastructure sector that I described earlier.

Improving how municipalities are managed and function on a daily basis must be a major priority for all local leaders. While some of the limitations on municipalities are imposed upon them by national and regional governments, others simply come from unquestioning acceptance of procedures whose original logic and importance is no longer relevant. Put another way, if we cannot justify current municipal practices in terms of present realities and challenges, we need to reconsider and to reform them.

5.4 Local Financial Systems

A fourth constraint is the weakness of financial systems for local investment. If we believe that most urban capital expenditures such as infrastructure, housing, or social services will provide benefits over generations, at least for 40 years, how can we finance them without sound local financial institutions? This must be a critical dimension of urban policy in a regional context.

Addressing these four constraints to the productivity of urban-based economic activities must be a priority for urban policy.

6. Supporting Multipliers

The second big issue I want to raise builds on the productivity issue: how do we support multipliers in the urban and regional framework? It is one thing to talk about productivity; it is another actually to create and support the economic multipliers that can improve productivity and job creation.

One of the most disturbing patterns of decision-making around the world is the continued focus on individual decisions by governmental units. There are repeated examples of how the infrastructure departments plan their investments without sufficient attention to the needs of those investing in industrial production or distribution. When I worked at the World Bank, I used to say that the people who worked on the 3rd floor believed that if the poor could have improved health services, they
would not be poor; on the 4th floor were the housing people who believed that if only the poor had housing they would not be poor, and of course the water people on the 5th floor believed the same thing. The problem was that these people only saw each other in the cafeteria or the elevators, but they rarely worked together in an inter-sectoral or cross-sectoral manner. In a real sense, the whole was less than the sum of its parts. Now I am sure this does not happen in your cities, but, who knows?

I would suggest that we all need to be much more aware that this problem affects us every day, in every institution. We need to apply practices within institutions which force units to be aware of each other’s work and needs. For example, why not have the approval of the budget of one unit depend on another unit, thereby forcing the first unit to be communicating and cooperating with the second unit. Or why not require that promotions and career advancement of officials in public institutions depend on serving in more than one department, so that people learn about the whole institution and do not become isolated in single departments. Of course, this rotation practice does not assure cooperative behaviour, but it raises our awareness of the problem.

A second approach to enhancing economic multipliers is to think about all of the links in chains of production, distribution, use, waste, and possibilities for recycling. By focusing on each link and examining how it can operate more effectively, we can learn about the needs of individual actors and institutions. An important part of this process is to understand the positive and negative externalities generated at each step. If they are positive, how can they be enhanced and increased? If they are negative, does the process of mitigation itself create opportunities for new kinds of economic activities which might employ people?

This approach is really an effort to pay more attention to the domestic or internal market in a region or a country. A recent book by a well-known American economics writer for The New York Times, Jeff Madrick, Why Economies Grow, argues that the process of economic growth is not primarily about trade and reaching out, but rather on deepening and building local, internal markets for goods and services. The challenge is how to build local institutions that support local production, investment, and growth. A good example of this is the creation of local banks in the West of the United States during the country’s agricultural expansion in the 19th century. If farmers did not have credit, they could not buy seed, and without seed, there would be neither crops nor income from the harvest. Small loans for agricultural machinery allowed increases in acreage and, later, economies of scale. Businesses to buy, sell, and service that machinery became an important urban function in agricultural regions. This then led to processing of agricultural products and new forms of agro-industrial development. This process laid the foundations for the prosperity of the American Midwest and for the American economy as a whole.

As we think about this story, we must remember that government permission and support for local financial institutions in the American West proved to be critical for strategic initiatives that led to the development of small towns and whole regions. All of those small towns we saw in cowboy movies from the American West were the result of those decisions!

Obviously, the same argument applies to providing working capital for small- and medium-sized enterprises in cities such as São Paulo. Facilitating that growth is a good investment by the public sector, because increased economic growth will generate higher tax revenues which can be used to fund investment as well as needed social expenditures for the least fortunate within society. Instruments such as infrastructure extensions, accelerated procedures for construction, or permits to start new businesses can all help this process to increase economic multipliers.

This argument has also been made by Jane Jacobs in her book, The Nature of Economies, in which she argues that economies, like biological organisms, grow through the process of differentiation. She develops the theory that economic activities in cities grow through the development of new products and services in response to changing demographic, economic, social, and environmental conditions.

An interesting example of this process has occurred in Buenos Aires during the past few years in the depth of the economic crisis. Desperate for some income, thousands of people living in the poor neighbourhoods on the periphery of the city would come into town at night and go through the garbage. They sorted the waste and started

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a huge recycling industry that had not existed before the crisis. What began as an informal activity has become increasingly formalized with the creation of recycling cooperatives; one recently even received a loan from the Inter-American Development Bank through the City Government of Buenos Aires.

These activities, however, modest, generate incomes and employment in areas needing stimulation. Understanding how one thing affects another is an important part of making strategic choices. An important advance in this understanding was demonstrated in 1998 by an American econometrician, George Galster, who studied the impact of changes in interest rates for residential mortgages and home improvement loans in 100 US cities. He discovered that interest rates affected patterns of home ownership and improvement, hence residential quality. Residential quality in turn affected investments in infrastructure and social services, including local public schools. The quality of public schools then affected the educational performance of children in those schools, with one result being the juvenile crime rate. He found very strong correlations between these factors and termed these patterns "cumulative causation".

In effect, what Galster demonstrated was that the inter-sectoral combination of strategic interventions tended to support one another and produce better, more sustainable outcomes. More importantly, he located these interventions in space, in a particular place. This point is of utmost importance, because it helps take us out of the realm of theory and immediately into practice, facing real people and their needs. Therefore, a critical part of the debate over urban policies must continue to focus on the importance of place and the opportunity that creating "good places" provides. The urban historian, Thomas Bender has argued that urban development:

...finds(1) realization in a place, in a specific spatial context in which...social processes and institutions intersect with the lives of the city's most vulnerable citizens. And it is in a place that over time and in the present those social burdens accumulate. We need to understand those places and make them better, for more than anything else city-making is place-making.  

7. Towards a Conclusion

This analysis suggests that the way urban managers address the central issue of employment and local economic growth can have enormous impacts on the state of welfare of urban populations. By focusing on densifying the local economic and social fabric, managers have the chance of weaving a tighter and more durable urban fabric. Perhaps the analogy is the Turkish carpet: those carpets that are more valuable have a higher number of knots per square meter. Surely, the high-density quartiers of Paris are also those of greatest economic and commercial value. And I am sure you can cite examples in Brazil and in São Paulo as well. While much of what I have discussed here is about economics and urban policies, I believe that the weaving together of these various strands of thinking and experience involves a high degree of artistry and craftsmanship.

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Mobilizing Public Finance for City Development and Management in African Countries
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1. Introduction: Background of the Problem

Urbanization in the last 20 years has become one of the most important trends in human settlement development and the prospects of all developing countries continue to be deeply affected by rapid urban population growth. While Africa was 80 percent rural in the 1950s and 1960s, its rate of urbanization now stands on average at 50 percent and the trend is expected to continue over the coming years (UNCHS, 1996). In West Africa for example, 50 million people are expected to migrate to cities over the next 20 years and it will take 80,000 hectares of land to accommodate them. It is projected that by 2020, 63 percent of the people will be living in cities. In Eastern Africa, the figure will be 55 percent.

A case of concern is the manner in which the urbanization process is taking place in the continent. A number of integrated forces are in operation. Firstly, the urban population and those moving to live in urban areas consist largely of unskilled labour. Secondly, municipal authorities, which were originally instituted as colonial administrative institutions, have not been structured to cope with the fast growing urban population (Beall, 2000). Thirdly, the existing revenue collection administration is generally inefficient and what is collected has, in some cases, been inappropriately managed. Finally, as municipalities are, in general, financially weak, they must rely on financial assistance from the central government, which only increases the leverage of the latter over them.

Policies towards urbanization appear to be changing, from a desire to control the growth of cities by curbing rural-to-urban migration, towards the acceptance of urbanization as an inevitable and even desirable process. Cities are now seen as the engines of national development, offering job opportunities and a higher quality of life to new urban dwellers. In South Africa, for example, cities generate over 80 percent of gross domestic product and are the key source of the bulk of government revenue. The 10 largest cities in the RSA have a combined municipal revenue of R40 billion per annum, which constitutes 75 percent of all municipal revenue in the country (RSA, 2001). It is worth noting that a few African countries, including Uganda, have begun to encourage faster urbanization as a way of inducing faster national development. This means that they have to be managed properly and funds provided to run them adequately, otherwise chaos would reign.

The last few years have also witnessed acceptance of the concept of sustainable development, which was adopted in Rio de Janeiro in May 1992 at the UN Conference on Environment and Development. As indicated in the Global Report on Human Settlements (UNCHS, 1996, p. 421), sustainable development brings together two major concerns: “meeting the needs of the present ... without compromising the ability of future generations to meet their own needs.” The first concern is about socio-economic development, while the second is about global ecological life-supporting systems. Within the urban context, the “needs of the present” include: firstly, access to an adequate livelihood or productive assets, as well as economic security for the vulnerable; secondly, access to healthy and affordable shelter and related services, including water, sanitation and domestic energy, as well as access to adequate healthcare and to education; and thirdly, freedom to participate in national and local decision-making processes.

As a result of rapid urbanization, pressure on urban services and facilities (the “present needs” as defined in sustainable development) has become a serious problem in many urban centres, and job opportunities offered by cities are too few for the large numbers of new urban dwellers. Consequently, the numbers of poor people in urban areas are rapidly increasing.

Due to this fast-paced urbanization, many African cities are now faced with a governance crisis at all levels, which is a result of the progressive weakening of public sector capacity brought about by a combination of state over-extension, ineffectual adjustment of external economic effects, natural events and poor management. Most countries have chronic budget deficits and cannot provide city services. It is the composite effect of these
failures that has necessitated significant emphasis on issues surrounding capability and capacity of local government.

Municipalities must thus confront a four-part agenda. First, they must manage available resources more efficiently and more responsibly. Second, they must be advocates for reforms in intergovernmental fiscal relationships, so that functional responsibilities are clearly defined and revenue sources are adequate. Third, they must mobilize new resources and increase their capacity to borrow responsibly for investments in local services. And fourth, they must seek ways of attracting private participation in the financing and delivery of public services.

Mobilization and deployment of financial resources is essential for sustainable urban development, not only in Africa but also in other parts of the world. But the prevailing economic situation has limited the ability of most central and municipal governments in Africa to raise enough revenue from traditional sources to fund new capital investments.

Finance is required for health centres, water and sanitation. It is also required for public goods that enhance the fiscal revenues of the local governments such as security, roads, education, public parks and so forth.

The management and financing of city needs will increasingly become the responsibility of city governments as more and more countries decentralize fiscal and administrative functions. Thus, city governments have a substantive role in financing capital improvements and facilitating local investment through the mechanisms available to them, including local revenue generated through tax and fee collection, public-private partnerships, equity sharing of capital projects, and incurring sector debt.

In this paper, we explore how African countries have fared in mobilizing public finance for city and municipal development through public finance. In this presentation we also examine the challenges these governments are facing and how these challenges can be overcome. The paper concludes by putting forward innovative ways of mobilizing municipal finances for development.

2. The State of the African Region's Cities

Africa's urban population will approach 550 million, or nearly 50 percent of its projected total of 1,187 million, by 2020. Today, urban areas account for 38 percent of the total population of 784 million and are credited with 60 percent of the continent's GDP. Municipalities, however, capture only one percent of the urban GDP, or US $6.00 to $8.00 per capita, as revenue. There is a similar disparity between the technical needs for municipal governance and staffing of municipalities.

Definitions of 'urban' and 'rural' differ widely across Africa. Many African countries use a population figure of 2,000 to make a distinction between rural and urban settlements. However, the figure varies from 100 in Uganda to 20,000 in Nigeria and Mauritius. Almost half the countries in Africa use an enumerative definition to indicate the areas that qualify as urban. The pattern of urbanization in West Africa differs somewhat from that in East Africa. In many West African countries, there are few secondary cities, so the population is concentrated in one or a few large cities. Population growth in East Africa is more evenly distributed over secondary and tertiary cities. This does not alter the fact that there, too, primary cities are growing through a period of rapid growth. By 2015, it is expected that two cities in Africa will have populations of more than 10 million and 70 cities will have populations of more than one million. The most important contributory factor to urbanization in West and East Africa is migration from rural areas to the cities. In South Africa, the natural increase in the population is the most important cause of urbanization.

The Economy of the City

The stalled process of globalization in Africa underpins the feeble nature of the formal economy in the majority of the continent's cities. In most countries of sub-Saharan Africa, regular urban wage employment opportunities constitute only a small fraction of total employment, typically between five and 10 percent. Regular urban employment has fallen in many countries, and elsewhere has failed to match the growth of the non-agricultural labour force. The slowdown in modern sector employment in recent years is linked to the fact that the public sector - as the engine of employment growth - has become increasingly unable to sustain the high rates of labour absorption from the 1970s and 1980s.
The impact of structural adjustment – which created shortages of imported materials, reduced investment, entrenched the public sector and led to declining effective demand – has meant that urban-based manufacturing has suffered particularly badly. Large-scale manufacturing, which created an impressive volume of jobs in Asia and Latin America, has generated only a small number of employment opportunities in urban Africa.

In Tanzania, public employment is the most important source of formal employment, especially in cities. In Luanda, Angola, employment in public service and state enterprises absorbs almost half of the working population. In Kenya, the public sector also accounts for about 50 percent of employment. Under structural adjustment programmes, public sector reform in several African countries has precipitated substantial layoffs. The current wave of public sector retrenchments in Africa has contributed to a downturn in urban jobs in particular. Women appear to have been most affected by the retrenchments and restructuring of the civil service.

Accompanying the faltering of public-sector-driven economies in Africa, there has been a sharp fall in modern sector wages in urban areas, especially, again, among civil servants. In Mozambique, for example, probably no family in an urban context is able to survive on the income derived from one of the 400,000 formal sector jobs.

3. Municipal Finance Experience in Africa

The fundamental problem of municipal finance in Africa is simply stated as the gap between financial resources and municipal expenditure needs, coupled by inadequate financial systems. This fiscal gap is growing in many countries because rapid urban growth creates increased demand for services, new utilities, maintenance, upkeep, and constant infrastructure renovations. Revenues collected by central governments and local authorities are generally insufficient. The fact that the growth of municipal revenue does not match the increase in urban economic activity is technically referred to as the lack of (municipal) income elasticity and this affects the majority of cities (Lohse, 2003).

Experience shows that in many countries, the taxing powers of local authorities are simply not wide enough and the yield from existing sources is often far too inadequate to meet their expenditures. Many cities in the African continent are largely dependent upon income derived from property taxation and other service charges, while other and more lucrative sources, such as income tax, sales tax, value-added tax and business tax are monopolized by central governments. Thus, many cities have to depend on central government allocations, which are themselves generally inadequate and often erratic in terms of timing.

For example, in the RSA, Parnell et al. (2002) indicate that local government derives its revenue from rates on property (19.9 percent) and trading services such as electricity (41.4 percent), water (11.8 percent) and sewage and refuse removal (8.22 percent). In addition, municipalities receive intergovernmental transfers in the form of agency payments, transfers to fund operational costs and capital transfers (averaging only 10 percent). While municipalities continue to receive income from these sources, national figures point to a crisis in municipal finance. “Project Viability”, a national cash-flow monitoring system, indicates that one third of municipalities are financially unsound. Over Rand 9.00 billion is tied up in outstanding debt to municipalities, and municipalities’ ability to honour creditors is decreasing.

Where local authorities are able to derive revenues from property taxes and service charges, meaningful tariff increases are sometimes refused or delayed by central governments for fear of eroding political support among the urban populace. In short, many governments continue to refuse to pay the political and financial costs of decentralization, that is, granting of more financial and decision-making powers to local authorities. Resolving these problems requires reconfiguration of central-local government relations, either towards more decentralized systems or more effective revenue sharing, and this can only be done if there is enough political will on the part of central governments.

A different set of reasons for the failure of urban local authorities to cope with increasing demands is to do with the characteristics of their existing sources of revenue and the inadequacy of the financial regulations and procedures employed. In addition to their inadequacy, many of the key sources of local revenues are generally inelastic, i.e., they do not have the capacity to yield additional revenue in proportional response to inflation, growth of personal
incomes and population growth. This, for a variety of reasons, is often the case with urban property taxes, the cornerstone of urban finances in many developing country cities—particularly those which inherited their systems from the British. A second reason, which affects the acceptability of some urban taxes and their long-term suitability, is that they are often regressive, thus failing to be effective instruments for redistribution and attainment of equity. The third reason is that many cities are lacking in administrative capacity and cannot, therefore, fully benefit from the existing sources of revenue. This is quite often the case with regard to property taxes, largely as a result of the absence of proper financial cadastres and the inability to carry out accurate real estate valuation and the necessary periodic revaluations. Collection of charges for urban services rendered may also be inefficient and many cities are owed large amounts of money by consumers, including central government and parastatal consumers.

The fourth reason is that some urban taxes are politically sensitive, thus affecting the willingness of local authorities to assess and collect such taxes effectively and to enforce sanctions on defaulters.

The fifth reason for urban authority failure is that financial transfers from higher government authorities sometimes lack transparency and predictability. At times, central governments fail to notify local governments of grants until well into the fiscal year, or central governments may effect sudden reductions. Regular formula-based transfers like those in Botswana, would be preferable to ad hoc grants for better long-term capital planning and budgeting by local governments.

Finally, poor financial management is contributing to municipal finance shortages. There are shortfalls in the capacity and technical expertise of local government to handle expenditure responsibilities and to generate revenue. An example often cited is inadequate administration of local property taxation. Studies in many cities have shown that urban administrators are often unable to update property valuation for tax purposes, mainly because of a lack of qualified staff and insufficient, poorly maintained records. One may add to this, various corrupt financial management practices—intentional under-valuation and over-allocation—leading to the inequitable generation and distribution of public revenue and to gaps where there should be none.

All of these problems affect cities in Africa, in varying combinations and to different extents. Yet, there are also some cities that have made some progress in improving their financing systems, in terms of revenue sources, collection systems, yield and financial management.

A number of cities and towns have, in recent years, embarked on wide-ranging reforms of their governance systems, including enhancement of financial mobilization and management capacity, from which useful lessons could be learnt. In Dar es Salaam, for example, the City Commission quickly realized that it had inherited from the elected City Council massive debts accumulated over many years due to poor collection levels and general financial mismanagement. To assist in raising the level of revenue collection, the Commission engaged the services of consultants to review the whole city financing system, assess the yield potential of existing sources of revenue and rationally determine new levels of rates, charges and fees.

In addition, a number of countries have set up specialized public finance institutions, which lend to local authorities for infrastructure investment. A few local authorities can borrow long-term funding from capital markets for urban development. Still, private capital markets appear to be developing rapidly (as RSA and, as conditions change, local governments in the future may tap these.

3.1 Sources of Municipal Revenue

Municipal governments across the continent derive their revenues mostly from internal and external sources. Of the internal sources, some are land-based in the form of property taxes and land fees, and the others are non-land-based like taxes on households and license fees of all sorts; whereas external sources are mostly revenue from intergovernmental transfers, grants, money from borrowing, donor funds from bilateral and multilateral agencies, etc (Lohse, 2003). In this section, we examine these sources, highlighting their value and adequacy to meet the ever-rising municipal needs of social and fine infrastructure.
Table 1. Sources of Local Government Revenues

<table>
<thead>
<tr>
<th>INTERNAL SOURCES</th>
<th>EXTERNAL SOURCES</th>
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<tbody>
<tr>
<td><strong>Land-Based Revenues</strong></td>
<td><strong>Inter-governmental transfers</strong></td>
</tr>
<tr>
<td><strong>Property Taxes</strong></td>
<td><strong>General purpose grants; Regular</strong></td>
</tr>
<tr>
<td></td>
<td><strong>transfers or formula-based shared</strong></td>
</tr>
<tr>
<td></td>
<td><strong>From governmental sources</strong></td>
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<tr>
<td><strong>Land Fees</strong></td>
<td><strong>Administrative fees, such as</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Grants for specified purposes</strong></td>
</tr>
<tr>
<td></td>
<td><strong>From private capital</strong></td>
</tr>
<tr>
<td></td>
<td><strong>markets (including international markets)</strong></td>
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</table>


3.2 Internal Sources of Revenue

3.2.1 Land-Based Sources of Revenue (a) Property Tax

The residential property tax is perhaps the ideal local tax in many ways. It is a rough form of benefit charge since landowners are primary beneficiaries from most local services. It is a tax best administered by local governments since it requires identification of each parcel of land, identification of each improvement, and identification of changes in ownership. In short, it requires familiarity with the local area. Clearly, the tracking of such changes is well beyond the reach of central government.

The property or real estate tax is one of the most common taxes levied at local level, but its potential is seldom exploited to the fullest extent. Property taxes in a number of African cities accounted for the following revenue percentages: 23 percent Harare, 23 percent Kariba, 27 percent Cape Town, 25 percent Durban, 16 percent Lagos and in Kenya, 25 percent in the town of Nyeri and 22 percent in Maragua town. (Olouwu, 2002; Lewa and Deva, 2004). Yet, property taxes should be the main sources of municipal finance (at least over 50 percent).

In most cases, valuation rolls are incomplete and out of date as in the case of Kenya, Uganda, Tanzania and Zambia. To make matters worse, default rates are quite high in some cities; for example the city of Gaborone was owed Pula 32.48 million (US $8.00 million) in 1999/2001. This relatively high sum could be used, for example, to provide much-needed housing for the city's poor.

The same holds in other cities in Africa, where the situation is chaotic in terms of reaping money from property tax. For example, Mika (2003), writing about the situation in the city of Berbera, Somalia, says that "Assets of the municipality were unknown and no balance sheets had ever been produced for the Somaliiland local authorities. No assets registers existed, nor were existing assets numberd. Further, there were no land management records like cadastral maps or sketches of streets. The number of properties in the city was unknown. Not all property was registered. Not all registered properties were billed, nor were all bills sent out. The grading system for property tax purposes was under the total control of the billing clerk." This was a recipe for chaos in municipal finance and it obtains in many municipalities across the continent today.

On revenue collection and billing, Mika found that not all the revenue bases were known, and the potential revenue was thus not being realized. Debt collection procedures were non-existent. The potential income was unknown. Expenditure and procurement controls were inadequate, while central government audits were not comprehensive.

Further, in most countries, central governments, which own many properties and use the services within the jurisdiction of urban local authorities, are supposed either
to pay rates in full or, more often, to provide grants to local authorities in lieu of rates; however, most do not pay, thus depriving municipal governments of substantial revenue. Finally, a potentially serious problem in most cities in Africa is the growing feeling, among city residents, that the money paid for rates and other local taxes is being poured into a bottomless pit, as it seems to have no impact at all in improving the quality of physical infrastructure and services. For example, in parts of Nairobi or Johannesburg, there have been suggestions that residents should suspend payment of rates and the service charge until such time as roads, water and sanitation begin to improve. It is likely that, increasingly, residents will demand to see results from the rates that they pay. This trend is likely to be encouraged by the political openness and democratic governance, which is increasingly characterizing African countries.

Property taxes are levied because the benefits of infrastructure and services provided by municipalities accrue foremost to the owners of property or their tenants. To raise more revenue from property tax in a way that is equitable, then technical expertise, the application of Geographical Information Systems, and institutional tax administration must be improved.

The legal formation of local improvement districts for financing community infrastructure is another common tool in some countries in the continent. In developing countries, a process that allows quick recovery of investment costs is land readjustment. Local governments, acting as developers, assemble public and privately held land for infrastructure provision.

However, the above problems are not insurmountable. For instance, at the national level some breakthroughs have been recorded in improved revenue mobilization through the creation of revenue authorities in many countries in the African continent. The few success cases involving property taxation include Accra and Lagos in the 1970s and 1980s.

As noted by Olowu (2002:25), the task of raising substantial revenues from the property tax hinges on three critical considerations. These are the political willingness of the crucial stakeholders; the opportunity as presented by the economic base and size of urban centres. The third consideration is capacity. The capacity to implement a property tax is dependent on the other two variables. If there is a willingness on the part of the key stakeholders—the political players at the central and local levels, private and civil society actors and donors—and if a country has cities of substantial size and economic base, then all the problems associated with the tax – valuation, assessment and collection—can be tackled with conventional technologies, but new technologies promise to enhance this capacity further.

Political willingness can only materialize if there are real incentives to those who wield power. There has to be an acceptance that the property tax represents an important investment over time to finance urban infrastructures, which are presently in crisis in much of the developing world. Given the problem of financing urban infrastructures in many cities and the breakdown in social cohesion (a real threat to the security of the rich and powerful), a programme of civil engagement on this subject can help to bring about a change in attitudes towards the tax. Donors who can make the development of the property tax a condition for grants and loans can further enhance this. Further decentralization in Africa would be more fruitful.

Since cities must rely on this source of municipal finance, more efforts should be made to collect as much revenue from this source as possible. Innovative attempts have been made by countries such as Botswana, where the City Clerk in Gaborone city once embarked on a campaign of ‘name and shame’ of defaulters. Names of defaulters and the amounts owed were published in the press and within no time, the city had raked in millions of money that was outstanding. Where defaulting continued, private debt collectors were called in. Results so far are quite encouraging.

(b) Land Value Taxation

Another approach to financing urban development is through land value taxation and resource rent. Land development and betterment fees can recover capital outlays for development work. However, very few countries in the continent have such fees. For equity and distributive reasons, it is logical that landowners provide returns on rising land values. Costs of providing new community services, or fees in lieu of services, may be recovered from large-scale developers at the time of development. These will, in turn, be recovered from resident beneficiaries.
Table 2. An Example: Sources of Revenue for City and Municipal Councils in Kenya (Kshs. Mil.)

<table>
<thead>
<tr>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Internally generated</td>
<td>2,252.17</td>
<td>2,736.97</td>
<td>2,938.21</td>
</tr>
<tr>
<td>Current Transfers</td>
<td>1.39</td>
<td>299.86</td>
<td>998.83</td>
</tr>
<tr>
<td>Sale of Goods &amp; Services</td>
<td>3,267.28</td>
<td>3,103.19</td>
<td>3,272.16</td>
</tr>
<tr>
<td>Loans</td>
<td>429.73</td>
<td>409.93</td>
<td>392.90</td>
</tr>
<tr>
<td>Total</td>
<td>5,950.57</td>
<td>6,549.95</td>
<td>7,602.09</td>
</tr>
</tbody>
</table>


through a higher purchase price or the creation of dues-paying associations of residents. Such taxes would function as user fees for what are essentially common heritage resources. Investment in land speculation is curbed, thus freeing funds for productive activities.

Taxing land sites according to land value promotes urban and rural land reform, providing affordable access to land for homes, businesses and farming. Sufficiently high resource rental fees, captured for public sector benefits, promote careful and efficient use of natural resources by the private sector. Conversely, under-taxation of natural resources leads to their over-exploitation. A high access cost for non-renewable resources can also stimulate investment in renewable energy and other sustainable technologies, as less profit can be made on extracting irreplaceable resources.

Several UN and other bodies (such as UN-HABITAT and FAO) have recommended this approach or urged its consideration. A paper distributed by the UN at the April 2000 Preparatory Committee of the Commission for Social Development also urged a land value tax as the “most immediately feasible way of coping with global poverty”.

When governments fail to tax land values adequately as they rise during development, and tax wages instead, workers soon cannot afford housing and other basic necessities unless they work longer or go deeper into mortgage debt.

There has been some experience with land valuation taxation in urban areas of the nations of Eastern Africa. Also, some cities in South Africa have had the benefits from collecting a portion of land rent as revenue. The Land Resettlement Minister of Namibia is currently working to implement this approach too.

3.2.2 Non-Land Based Revenues

The second source of municipal finance is money from non-land based revenues. Across local governments in Africa, there are significant differences in how much municipalities earn from non-land sources of income. These sources are examined below.

(a) Tax on individual income

Income tax, as a source of revenue, currently exists in a few countries such as Uganda and Tanzania. But even in these countries, there are poor records of both employees and employers, even in the formal sector, and so the yield is low. Partly because of poor record-keeping, local authorities resort to charging flat rates for self-employed persons, thus introducing a significant element of inequality.

(b) Local taxes

Experience shows that local tax systems in the continent have remained as they were in many countries in the colonial period. The poll tax and octroi belong to this category. These taxes bring problems of horizontal and vertical equity; large numbers of public service employees are excluded. The octroi is like a city-based import-export tax and, therefore, a constraint to trading, while the poll tax in the country where it is most developed has been found to be inefficient on an input-output basis (Livingstone and Charlton 1998).

The problem with local tax is collecting it and, secondly, local tax capacities do not exist in many countries. The fact of the matter, though, is that only a few large corporate operators, and mainly public operations and employees, fall into the tax net. The mass of others pay no taxes whatever. Hence, the idea of a local income tax is not an attractive one as national governments still confront
serious difficulties to collect other direct taxes (Olowu, 2002).

(c) User Charges

Service or user charges are today a much-discussed source of municipal revenue in Africa, though in many cities these are not heavily utilized despite their many advantages, the large number of services upon which they can be readily imposed, and evidence of willingness to pay. With a few exceptions, local governments in Africa rely more heavily on taxes to fund local government expenditures than on user charges.

Charging immediate users of infrastructure and services has become a common principle, and user charges are growing in importance worldwide. User charges are designed to generate revenue to cover operating and investment costs. The system provides for more efficient municipal services and infrastructure and enables rates to be set and adjusted at levels that reflect real capital costs, finance charges and inflation. Where independent institutions, such as independent public or private water, sewerage and electricity utilities, establish fee levels and handle revenues, financial self-sufficiency can be achieved, as has been shown in some countries. Cost sharing has been introduced in services provided by municipal governments such as education, health, etc. However, experience shows that the charges are too low and inadequate for effective provision of such services.

A general problem affecting a number of services provided by local authorities in many countries is undercharging. Further, charge rates are infrequently revised, rendering charging services, as a source of local income, inelastic. Inefficient billing in some cities, for example in Nairobi where water billing is often behind, exacerbates this. User charges in many countries have not changed, and have declined in real terms, for more than 15 years (Fox, 1994).

Of course, in order for user charges to be imposed on public services, there must be a willingness-to-pay (WTP) on the part of the consumers. There is much evidence suggesting that people in Africa pay a much higher price per unit of service when acquiring services from private vendors than they would pay in user charges if public provision were available. For example, in surveying 395 households in Nigeria, it was found that the amount households were paying for vended water was approximately equal to that paid in industrialized countries for much higher quantity and quality of water services (Mu, Whittington and Briscoe, 1990). Reedy (1986) conducted a similar survey, finding that low-income households in Lagos, Nigeria pay private vendors four to eleven times the marginal costs of public water delivery in that city. Another survey of research in nine developing countries (Whittington and Choe, 1992) revealed that expenditures for water provided by private vendors represented more than 10 percent of income.

The successful application of user fees also requires a convenient way to measure individual consumption. Increasing user fees to economically efficient levels should be the first priority of an infrastructure strategy. Care must also be taken to avoid excluding the poor from services because of their inability to pay. Cross-subsidies (as used in Botswana) are often used in several countries in the continent to create a more progressive schedule of fees (Fox and Edmiston, 2000).

User charges financing is more economically efficient than tax financing whenever it is possible to price services. User charges have the potential to be the most reliable source of funding those services that can be priced. Tax revenues or intergovernmental revenues are much less likely to provide a consistent source of competing uses and can diminish available resources. Local governments in developing countries have found that intergovernmental revenues are a particularly erratic revenue source.

If user charges are to be the major funding source for service delivery, they must be high enough to finance service delivery. In most instances, user charges will raise adequate revenues if the price is set equal to marginal cost.

More aggressive imposition of user charges in Africa would provide a substantial boost to public coffers. Anderson (1989:529) calculated the potential contribution to public revenue of levying user charges on electricity, water, telecommunications and roads in several African countries. He concluded that a 25 percent increase in public revenues was a realistic possibility.

User charges also have great potential for funding additional investment in public service infrastructure. Anderson (1987) demonstrated that if user charges increased the financial rate of return to public services
infrastructure by five percent, enough revenue would be generated in Sub-Saharan Africa to finance a 60 percent increase in annual capital expenditures.

In addition to financial benefits, there are many other benefits from imposing user charges. User charges have the potential greatly to improve the public sector’s efficiency, to impart a more equitable distribution of the financing burden of public services, to provide better information regarding infrastructure needs, and to improve the quality of existing services.

**Practical Issues of User Fees and Tax Collection**

African countries often fail to collect substantial user charge revenues primarily because of inadequate billing procedures, inadequate enforcement of payment and outright theft. Payment should be enforced through late fees or disconnection for non-compliance, though such mechanisms are frequently not used. Moreover, public enterprises in Africa are severely understaffed, so even if enforcement mechanisms are in place, consumers may not be compelled actually to pay.

Some people engage in theft or illegal tap-ins in places where collection is enforced. Illegal connections have been observed to account for losses of 20 percent of total water supply and electricity output in Africa (Anderson, 1989). Theft and illegal tap-ins can be reduced through combinations of different technologies and better enforcement.

Breaking of meters presents another collection problem. For example, meters are in place for most water delivery subscribers in some Egyptian cities, but a substantial percentage of these meters are inoperable due in large part to their being destroyed by subscribers (EHP, 1995). Once user charges are collected, there can be problems in making the revenues available for delivering the service. Given the large deficits faced by most governments in Africa, there is political pressure to transfer user charge revenues to the general fund of the government. The service quality will suffer, leading to a diminution of willingness-to-pay, if there is no linkage between service delivery and revenues. Earmarking of user charge revenues is necessary to ensure that the funds are available to finance the public services for which they were collected.

Revenues collected above the necessary delivery costs should go to the government’s general revenue fund, not to the earmarked pool. World Bank data for road user charges in sub-Saharan Africa provide evidence that user charge revenues are often not entirely earmarked for service maintenance and improvements. RUC revenues are being shifted to public purposes other than road service in all countries, as seen in Table 3. Possible results include erosion of infrastructure if services are not maintained, or failure to expand the capital stock.

Finally, potentially severe political problems are associated with taxing user charges. As mentioned earlier, imposition of user charges is likely to be protested by consumers. Levying taxes in addition to the user charges will only exacerbate the situation.

**Table 3. Road User Charges in Selected Countries and their Relation to Expenditures**

<table>
<thead>
<tr>
<th>Country</th>
<th>Year</th>
<th>RUC as % of Road Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kenya</td>
<td>1981</td>
<td>138</td>
</tr>
<tr>
<td>Mauritius</td>
<td>1981</td>
<td>1700</td>
</tr>
<tr>
<td>Somalia</td>
<td>1979</td>
<td>411</td>
</tr>
<tr>
<td>Sudan</td>
<td>1981</td>
<td>269</td>
</tr>
<tr>
<td>Uganda</td>
<td>1984</td>
<td>411</td>
</tr>
<tr>
<td>Zimbabwe</td>
<td>1983-84</td>
<td>345</td>
</tr>
<tr>
<td>Cameroon</td>
<td>1978</td>
<td>273</td>
</tr>
<tr>
<td>Sierra Leone</td>
<td>1979</td>
<td>200</td>
</tr>
</tbody>
</table>

Source: World Bank (1987); See also Anderson (1989)

**Equity Considerations**

Equity is a very important consideration of public administrators in Africa, as in all parts of the world. Many of the justifications that are given for financing public services with taxes rather than user fees result from the perceptions by some that user charges are unfair. Equity is a very complex issue, and in many regards, the equitable nature of differing revenue collection policies lies in the 'eyes of the beholder'.

One potential method for raising progressivity of user charges is to impose rising block tariffs. A rising block tariff is a user charge structure in which consumption up to a specified amount is priced at a very low rate, while additional
'blocks' of usage are priced at increasing rates. This system is used in pricing water in urban Botswana. Rising block tariffs have the potential to impede redistribution of the revenue burden to those with relatively higher incomes, since low-income people consume less public services than do high-income people.

(d) **Tax on provision of goods and services (license fees)**

Tax on provision of goods and services, which is generally in the form of trade licenses and fees, is an important source in most countries. However, in some instances, increasing license fees has proved to be very difficult and politically sensitive. Collection and follow-up of defaulters has also proved to be problematic.

(e) **Income-generating enterprises**

Income-generating enterprises are not a significant source of local government revenues in Africa, and appear to be getting less and less popular with the increasing preference for privatization. The method is practiced in Tanzania, Kenya, South Africa, Zimbabwe (mostly from opaque beer-brewing and running of beer outlets) and Nigeria among others.

(f) **Public-Private Partnerships - Privatisation**

Several municipalities in Africa have embarked on public-private partnerships (PPPs) or complete privatization to raise money to finance projects. For example, as a way of servicing land for housing, the Harare city council embarked on a PPP policy in November 1987 and has achieved some notable results. The same has happened in Botswana, where the city of Gaborone has also gone into partnerships with several firms for land servicing and residential development. Water has been privatized in many countries, including South Africa, Tanzania and Ghana; so too, has been waste removal in many East African cities (Nairobi and Dar es Salaam).

An important aspect of privatization is the fact that investment in infrastructure development can be taken over by the private sector. Urban growth requires large capital investment in infrastructure such as transport, water supply, sanitation and other network systems attractive to private companies.

Two types of privatization of urban services have emerged over the last decade. The first type is what might be called "spontaneous privatisation." This has arisen in an attempt to fill-in the increasing gaps left by local governments. Because of the deterioration of existing services and the lack of expansion to cater for increasing urban populations, private providers of services have emerged without any initial prompting from either central or local governments. This has been particularly so in the case of water supply, mainly in the form of private water kiosks in many low-income areas. This has also extended to solid waste removal in high-income areas. A second type of privatization of urban services is more formal and organized in most cities in the continent.

The partnerships have helped promote governance at the local level through:

- Expanding interaction between city governments and other key actors in the urban economy;
- Sensitization on the needs and capabilities of the urban population, especially the urban poor, the city councils and sector ministries.

Although efficiency generally has improved, there are shortcomings about privatization of social services. Evidence suggests that many urban poor people are unable to pay even the minimum charges required for basic education and health services. In other instances, private contractors usually operate mainly in middle- and high-income areas, where residents can afford to pay, leaving many of the poor without such services. In a number of countries, including Cameroon, Côte d'Ivoire, Guinea, the Republic of Congo and Senegal, public municipal bus companies are disappearing with the privatization of the transportation sector. Private taxis and bus companies often are more expensive, and serve the more lucrative routes, forcing many urban residents to cycle or walk longer distances.

The current Executive Director of UN-HABITAT sees a role for privatization of water services, but also raises concerns about equity and access. "It is a myth that the poor at the moment are accessing water for free," she argues. "Because of a total failure of public provision, the water is not reaching these people". As a result, they must buy water from informal sector vendors, and often end up paying more than the rich do. "The notion of privatization of water services is, in itself, not a bad thing." But then, she adds, "How will people access the privatized water?" Policies are needed to ensure that the poor are not
excluded simply because they cannot afford to pay. "It is not a matter of either/or. It is a question of finding clear answers, without losing sight of the end objective, which is to improve people's access to water" (Harsch, 2001). In Uganda, for example, the government's long-term goal is to ensure full "cost recovery" for municipal services. But it also recognizes that public subsidies may be necessary to ensure that low-income groups have access to clean water services.

In sum, a crucial privatisation issue is ensuring that access to essential urban services is open to everybody and that low-income groups are not discriminated against. Therefore, there is no doubt that the public sector should retain an important role in controlling and supervising the provision of infrastructure and services by private enterprises. Private sector management of operations with close control by local governments, including mandatory cross-subsidization, is a widely accepted solution. Cross-subsidies are currently used in Botswana where serviced land is allocated to people according to affordability. It works like this: low-income people are charged subsidized rates, middle-income people are charged cost recovery rates and well-to-do users are charged market rates. This way, the municipalities do not carry the burden of land servicing, and the rich subsidize the poor.

3.3 External Sources

3.3.1 Central Allocations or Inter-governmental Transfers

In many African countries, sub-national governments are given relatively little taxing power. The major source of local government revenue in these countries is intergovernmental transfers from the central level. Botswana is a good example. In the 1995/96 budget, Revenue Support Grants represented 64 percent, 92 percent and 91 percent of recurrent income for Urban Councils, District Councils and Land Boards respectively (Mosha, 2001). In this case, local governments cannot set the tax rate or define the tax base for most of the major levies; therefore, they have little control over the total level of revenues available.

Intergovernmental transfer systems can be decentralised to varying degrees:

- By guaranteeing local government revenues an adequate flow of revenues.
- By providing local governments with some degree of certainty in the flow of revenue, so that more efficient fiscal planning is allowed.
- By providing local governments with transfers that have no "strings attached", i.e., by giving unconditional rather than conditional grants.

To evaluate the degree of centralisation of the grant pool, one might think of two dimensions of a grant system: the method of determining the size of the total pool of distributable funds, and the method of allocating the funds among the eligible units.

The size of the total grant pool might be determined in one of three ways: (a) as a share of a national tax, (b) on an ad hoc basis, and (c) on the basis of cost reimbursement. The former has the potential to be the most decentralised, in that it can guarantee the local government some significant flow of revenue (assuming that the centre does not change the rules for distribution). The other two forms of determining the distributable pool are more centralising.

The ad hoc method lets the central government determine how much will be allocated to local governments in any given year. The local governments, therefore, will not have an "entitlement", and local voters will see the size of their budgets as beyond the control of locally elected officials. The cost reimbursement approach, likewise, will not be very centralising, because it allows the central government to set standards for locally provided services, and to direct investment toward those services where national priorities are the greatest.

Practice shows that in most African countries, revenue-raising powers are placed at national government level, though municipalities in many countries have significant own taxes. Several systems exist for transferring funds to local authorities. In Botswana, for example, urban authorities get 100 percent of the development budget and between 40-60 percent formula-based of their recurrent budget from the central government (Mosha, 2001). In other countries, the situation is as follows: Kenya has formula-based block transfers to local authorities; Malawi uses general-purpose, block transfers or specific-purpose, formula-based transfers; in Nigeria, federal transfers are formula-based whereas transfer programmes to the
Local Government Agencies have been historically very unpredictable; and lastly in Uganda, the 1995 Constitution certifies unconditional, conditional and equalization grants. Details of a few selected countries are given below to illustrate the extent of capital transfers, viz:

(a) In South Africa, as seen from Table 4, local government does receive fiscal transfers from national government, but collects a substantial proportion of its revenue, and also borrows money for financing part of its capital spending. Municipal councils raise 90 percent of their own revenues mostly through bulk purchasing of retailing of water, electricity and sewerage services and property taxes (19 percent) and other fines and fees (18 percent). They receive only 11 percent of their revenues from central (four percent) and regional (seven percent) transfers. The six metropolitan municipalities are largely self-financing (receiving three percent to 6.7 percent of their budget grants), while smaller and rural municipalities with weaker tax bases are much more dependent upon transfers (receiving up to 87.3 percent of their resources from transfers). Municipalities have been historically major players in governance and also quite autonomous. The same cannot be said of the rural municipalities. According to the Constitution, local government and each province are entitled to an equitable share of revenue raised nationally to enable them to provide basic services and perform the functions allocated to them. The transfers are formula-driven, based on objective criteria, well publicized, and determined well in advance (van Rynve 2005:6). An important lesson from South Africa’s experience is that it is indeed possible to raise substantial revenues from user fees and property taxes.

(b) In Ethiopia, inter-governmental transfers are made on the basis of a formula that considers some variables like population numbers, level of development and the revenue-generating capacity of regions. The level of development of regions is identified in terms of various indicators of social and economic infrastructure, urban population, industrial production, food crop production and summarized in an index called I-distance. Among these three variables, two — population number and levels of development — are designed to reflect the equity issue in allocating resources. The weights given to the different variables change from year to year. In 1996/97 for example, the weight attached was 33 percent to each of the parameters: population number, level of development and revenue-generating capacity. In 1997/98, the weights attached were 60 percent for population number, 25 percent for level of development and 15 percent for revenue-raising efforts. The formula allocates higher shares to those states with large population sizes such as Amhara, Oromiya and SNPP, although the shares are not completely equivalent to their share in the total population. The less developed or ‘emerging’ regions receive higher subsidies on a per capita basis than the other regions.

(c) In Tanzania, in a move to strengthen the revenue base of the local authorities, the Local Government Finance Act was amended in 1999 to appoint local authorities to be licensing authorities in respect of the business of commission agents, manufacturers’ representatives, brokers, travel agents, buying and selling motor vehicles, import trade, regional trade, companies, cooperative societies and so forth. The fees collected are to be treated as revenue accruing from the local
authorities concerned. Legislation was also amended to require the central government to make block grants to local authorities to meet the cost of development and maintenance of services, particularly education, health, water, roads and agriculture. Block grants may vary from one authority to another depending on the grades, and the Ministry of Local Government may prescribe standards as desired. Under the LGFA, local authorities are empowered to borrow money or to draw bank overdrafts as long as they get approval from the Ministry of Local Government, which consults with the Ministry of Finance. Nevertheless, local authorities in Tanzania have not been active borrowers of finance in the open market.

(d) In Botswana, apart from what has been detailed above, it is observed that the financial dependence of local authorities upon the centre is the single greatest barrier to decentralization. It breeds an unhealthy reliance upon the government, forcing local authorities to look to the centre for advice and direction even on the smallest matters. This reverses the direction of accountability, making local authorities less responsive to the demands of their constituents. This is in spite of government policies whereby "...Decreasing the financial dependence of municipal and district councils and land boards upon central government, and thereby increasing their autonomy and accountability to their own constituents, is the primary policy goal of MLG and the current six-year development plan" (Mosha, 2001).

(e) In Kenya, resource allocation is centrally done, except for the Local Authority Transfer Fund (LATF), a central local transfer facility that supports local delivery of services to the local authorities. The country’s poverty reduction strategy paper has, overall, provided for a one-year period for the development of a decentralization policy, which would ease access and control of financial resources (amongst other resources) at local level.

(f) In Uganda, with the attainment of decentralization, local government has gained autonomy to manage their own financial and planning affairs. This has significantly changed the relationships between central and local government. An established Local Government Finance Commission of seven members advises the president and local government on financial matters. This commission recommends the amounts to be allocated as various grants to each local authority. It also advises the local government on appropriate tax levels. The commission is independent in its operations, which is important for objectivity in handling local government financial issues.

The Kenyan government retains the powers to determine the type of taxes to be levied by local government. It also prescribes the financial controls and accountability measures for compliance by local government, including regular audit and inspection. Local governments share their revenues in agreed proportions, and in accordance with the law. In the city and the municipal councils, revenue is collected by the division councils, which retain 50 percent of all revenue collected and remit 50 percent to the city or municipal council. The city or municipal council is, however, required to distribute at least 30 percent of its total amount of revenue to the division councils in its area of jurisdiction. This acts as a mechanism for equalization among the division councils in each city or municipal council.

In rural areas, the sub-county councils collect revenue. They retain 65 percent and remit 35 percent of the total revenue collected to the district council. The sub-county council redistributes the amount it retains to the county council (five percent), the parish council (five percent) and the village councils (25 percent) and retains the rest for its own operations.

Kenyan law provides safeguards against non-remittance of the agreed percentages. The district local government and municipal councils are also required to provide the necessary guidance and technical support to the lower-level local governments within their areas of jurisdiction, and enforce the principles of financial management and accountability, including conducting internal audits and regular inspections.

Other countries - In other countries, municipalities get little from the centre. For example, the city of Harare gets barely a one percent contribution from central government in the form of grants through the Public Sector Investment Programme-PSIP (Kinyungu, 2004). There is a separate budget for capital expenditure based on the Capital Projects Programme. The sources of capital finance are derived from various funds set up by the Council, i.e., the Consolidated Loan Fund (75
percent), the Capital Development Fund (15 to 20 percent), the Estates Account (six to eight percent) and Service Connection Fees. The contribution of these funds and sub-funds to municipal capital expenditure has tended to vary over the years.

A major problem in some countries is the uncertainty characterizing central government allocations. Local authorities are never certain about when they are going to receive their allocations from central government, or about how much they are going to get. Another problem is the central government’s distrust of the competence of local authorities. They do this to cling to the financial muscle. Even where transfers are adequate and reliable, a fiscal regime which compels local actors to depend so heavily on central financial arrangements for practically all of their expenditure requirements undermines the development of lateral rather than vertical relations within the state, with serious implications for public participation and effective accountability.

3.3.2 Intergovernmental tax sharing

Most African local authorities, including municipalities, get revenue from tax money collected by central government. In Kenya, 20 percent of the tax levies on road fees and five percent of the annual income are normally shared; in Uganda, according to the Local Government Act of 1997, 35 percent of the total collections have to be transferred to districts. A formula-based revenue-sharing scheme is also available in the Local Government Act for the distribution to divisional councils of revenue collected by the municipalities and cities; in Nigeria there is general revenue-sharing of national revenues in the Federal Account, but in countries like Rwanda the system is not clear and lastly, in Malawi, there is no inter-governmental tax-sharing system in operation.

3.3.3 Sub-National Borrowing: Efforts to tap the Private Sector

(a) Money from national or commercial banks

Experience across the African continent has shown that municipal urban infrastructure projects have largely been financed by central governments and lending by higher levels of government. Since the demand for local infrastructure finance is growing faster than the supply from these traditional sources, it should be useful to examine various innovations which local municipal governments have adopted to tap private resources in order to finance their revenue-generating projects. Also, the increased administrative autonomy resulting from a regime of decentralized governance encourages more private sector-led development of local projects.

In some countries in the African region, sub-national governments, like municipalities, can borrow to finance their development programmes. A few examples where this is practiced are Zimbabwe, South Africa and Uganda. In Zimbabwe, this has been a great success. For example, as from 1990, the largest building society in Zimbabwe, the Central African Building Society (CABS), has provided the City Council of Harare with loans for off-site services at reasonable interest rates of 14.5 percent and 22 percent with the payment period stretching over eight and 15 years respectively (Kinyungu, 2004).

In the case of Uganda, local authorities are allowed to borrow from the banking system within the constraints imposed by the Local Government Act of 1977, although there has been little borrowing thus far. In Kenya and Botswana, there is virtually no borrowing, due to past heavy debts and problems with repayments.

In South Africa, municipal borrowing stood at R12.4 billion in March 2004, and the key lenders have been the Development Bank of Southern Africa with loans to metropolitan authorities of a little over five billion Rand, and a private sector lender, the Infrastructure Finance Corporation (INCA), with loans of just under three billion Rand. Other private banks account for most of the remaining amounts.

The South African government has set conditions for financing infrastructure through borrowing by:

- Avoiding national government guarantees

If municipalities are able to borrow from the private financial sector at reasonable rates, lenders need to be assured of being repaid. This can be done either by national government guaranteeing repayment of loans, or by ensuring that the finances of local governments are sufficiently rigorous that such guarantees are not required. The South African approach has been to avoid guarantees. Policy-makers and administrators have thus sought to create the conditions for borrowing within this context. This has required great

Enhancing Resource Allocation to Urban Development in Africa
emphasize to be placed on creating the circumstances for the emergence of sound municipal finances while promoting autonomous local government.

- **Ensuring sound municipal financial management**
  This has been through creation of an overall sound local government framework.

- **The Municipal Finance Act**
  The Act places great emphasis on clarifying accountability and ensuring transparent processes, so that key fiscal decisions are required to be made public.

- **The New Municipal Infrastructure Grant (MIG)**
  This is intended to place a greater emphasis on the achievement of outputs as opposed to inputs. MIG is focused on achieving a number of output conditions, including the achievement of service coverage targets, employment creation and the linkage of integrated development plans to budgets (van Rynseld, 2005).

**Table 5. South Africa: Borrowing by Metropolitan and Other Municipal Governments - March 2004**

<table>
<thead>
<tr>
<th>Name of Municipality</th>
<th>Total External Borrowings (R Millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cape Town</td>
<td>2,653.3</td>
</tr>
<tr>
<td>Johannesburg</td>
<td>3,842.8</td>
</tr>
<tr>
<td>Tshwane (Pretoria)</td>
<td>1,539.9</td>
</tr>
<tr>
<td>EThekwini (Durban)</td>
<td>3,085.4</td>
</tr>
<tr>
<td>Ekurhuleni (East Rand)</td>
<td>1,068.4</td>
</tr>
<tr>
<td>Nelson Mandela (Pt Elizabeth)</td>
<td>296.9</td>
</tr>
<tr>
<td>TOTAL</td>
<td>12,486.7</td>
</tr>
</tbody>
</table>

Source: van Rynseld (2005:10)

(b) **Getting Funds from Africa's Capital Markets**

The capital market is reckoned to be the largest source of private capital in both equity and debt. It exists in most African countries in various forms, including savings accounts, balances in commercial banks and savings societies, savings in national social security and pension funds, insurance life funds and compulsory savings schemes.

Shelter Afrique, a regional housing finance institution based in Nairobi, Kenya, was set up by African governments and the African Development Bank to promote housing and urban development in Africa. It provides debt and equity finance as well as technical assistance to both private and public institutions for housing and related development. The company finances projects that extend urban services, improve living conditions and increase the housing stock through private and public housing institutions. It has sought credit from multilateral development institutions, international banks and donor agencies as well as capital markets.

In 1998, Shelter Afrique had to change its resource mobilization strategies by targeting local capital markets. The company decided to make contributions towards developing the capital markets as a source of housing finance.

Shelter Afrique’s experience is that African markets have matured to accept debt instruments not only for corporate financing but also for urban and housing services. Municipal authorities must, however, be prepared to meet the requirements imposed on corporate entities.

Another success is the case of municipal bonds in South Africa. The new municipal bond market is emerging in the context of no prescribed asset requirements, no national guarantees, and no tax benefits for municipal bonds. Indications are that this market could become a very important source of future financing for local government.

For example in 2004, Johannesburg successfully floated two bonds of one billion Rand each to fund its projects. Capital markets in many African countries are well developed and could provide sustainable sources of finance for urban services and housing. Most city and municipal governments run budget deficits of over 80 percent of their revenues, regrettably to finance recurrent expenditure with little left for capital expenditure. The capital markets could enable municipal government to raise the funds needed for current developments against expected cash flows.

Central governments also have a role to play. Decentralization of services to the local governments must be accompanied by further legal, institutional and financial support to enable them to execute their mandate. Some local governments may also need the support of the central government to access capital markets. The current situation where the central government commands all
the credit available in the market to meet its insatiable demand for funds would not help in the development of the corporate and sub-sovereign debt segments of domestic financial markets.

(c) Other Funding Options

Two other options are being explored by housing and municipal finance specialists – the Guarantee Fund and the Challenge Fund.

Commercial banks are the primary source of housing finance in the private sector. But these banks deal mainly with the higher-income bracket and the challenge is how to lower their threshold. One way of meeting this challenge is to use Guarantee Funds. The idea of establishing an international guarantee facility for shelter development builds on the past experience of the USAID Housing Guarantee Programme. Such a facility would guarantee domestic loans (in local currency) and make housing finance more attractive to national banks and local financial institutions. The same global guarantee facility could also be used for municipal infrastructure. Some pilot testing would be very useful in this area, in collaboration with municipal banks and utility providers.

An example in Africa is the National Urban Reconstruction and Housing Agency (NURCHA) of South Africa, which was established in 1995 to guarantee home loans that commercial banks offer to the lower-income bracket. South Africa has established a stable financial system and four major commercial banks deliver more than 70 percent of housing finance. This situation leverages the effectiveness of the guarantee scheme.

The second course of action would be the establishment of an international Challenge Fund for slum upgrading. The concept of “challenge funds”, designed to provide financial incentives for good initiatives, received a strong boost at the Monterey Conference on Financing for Development in March 2002. Such challenge funds do not involve high management costs as they provide grants to institutions or programmes. These grants are usually based on conditionality and competition. They can and should be used to leverage municipal and national resources. A Challenge Fund would provide substantial financial support to municipalities committed to abide by the guidelines issued by UN-HABITAT and ready to implement large-scale operations. Such incentives may cover only a small part of the costs involved but they could be highly publicized, for instance through an annual award system.

(d) Money from International Donor Agencies – Grants or Part Loans

A number of countries in the African continent rely a lot on donor money (credit or part credit and part loan) to finance various projects in their municipalities. The vast majority of the projects involve infrastructure like water, electricity, roads, sewers and housing projects, especially slum upgrading. The funding emanates from donor agencies, including various United Nations bodies and UN-HABITAT, the Ford Foundation, from bilateral loans from various countries in the Western hemisphere and lastly the World Bank, which provided a large amount of funds in the 1970s and 1980s for site and service projects.

For example in slum upgrading, UN-HABITAT and the World Bank launched the Cities Alliance in 1999, which has been spearheading the “Cities Without Slums” initiative. The campaign works with other UN agencies, regional development banks, bilateral donors, local associations, NGOs and private companies to identify and prepare citywide and countrywide slum upgrading programmes. In Africa, such plans have been prepared for Mauritania and South Africa. The grant facility's total for the first three-year period (1999-2010) is US$40 million (Harsch, 2001).

Assistance for the development and management of human settlements has also been a key mission of UN-HABITAT during the last 20 years. The Technical Cooperation Division has implemented more than 1,000 projects in developing countries (Africa included) representing a total of US$1.0 billion. These projects have contributed to the definition of new housing and urban policies consistent with international agreements, such as the Global Strategy for Shelter to the year 2000 and the Habitat Agenda. In some exceptional cases, they have included the provision of seed capital for low-cost operations, in collaboration with the UN Capital Development Fund (UNCDF) and UNDP. Funding for these technical cooperation projects has mostly been mobilized on a case-by-case basis at country or city levels, from UN and non-UN sources (Biau, 2003).
Further, in another example, the World Bank has been supporting the urban sector and municipal finance in South Africa for decades. In the early 1990s, Bank support focused on helping the black townships. The government’s Municipal Infrastructure Grant has evolved into a transparent, predictable, poverty-targeting subsidy mechanism that currently funnels over US$1.00 billion annually to poor communities.

The Municipal Financial Management Technical Assistance Project, amounting to US$15 million, is the only active World Bank loan to South Africa. It supports the building of financial management capacity for more than 40 key municipalities around the country.

In addition, the World Bank assists the South African Cities network through Cities Network grant support for municipal knowledge development strategies. The nine largest cities in South Africa account for over 60 percent of GDP, and South Africa accounts for 40 percent of the Sub-Saharan economy (World Bank, n.d.)

The concessional loans for shelter and urban development provided by international development banks to national governments certainly remain useful and welcome. However, they have a built-in limitation: they are made and reimbursed in hard currency while housing and infrastructure are essentially a domestic asset. Therefore, in spite of their usefulness, these existing loans cannot be the only response of the international community to Target 11 of the Millennium Development Goals.

Lastly, in many countries local governments/municipalities are also not allowed to hold ‘donor round tables’ at the local level in order to directly discuss with ‘donors’ the type of support they require. This inability to raise/negotiate funds directly is commonplace in many West African countries except notably Senegal (although a limit is placed on the amounts of money that can be transferred directly to a local government); it means that most local governments still rely on national ministries to tell them what to do and how to do it (conditionality of funding). This might work if local governments were involved in the discussions to set up such conditionality, which is not the case. This type of ‘constraining order’ on local governments does not allow much leverage in resource-poor settings to respond to real local priorities that may not make the national priority.

(e) Money from NGOs to Finance Urban Development

Several countries in the African continent have accessed money to finance their urban development through nongovernmental agencies of all sorts. For example, Habitat for Humanity has been building shelter for the needy in Africa and elsewhere, producing over 20,000 houses per year in some 80 countries. In Kenya, the NGO has housed 1,300 families, and the current cost of a house ranges from US$550 to US$1,100. It has created a “Fund for Humanity” designed to revolve in the community, providing beneficiaries with non-profit, interest-free loans whose repayments provide others the same opportunity (McCann, 2003).

3.4 Major Challenges for Mobilizing Funds for Municipal Financing

3.4.1 Problems of revenue collection at the local level

Municipal government’s ability to generate revenue through taxation is severely limited because central government insists on the prerogative of imposing taxes and determining tax rates. The only substantial revenue source, which is almost universally at the disposal of local authorities, is property taxation. Although this is the most important single source of human settlements financing accessible to local authorities, it has shortcomings in its potential to increase revenues. Since the tax base – the amount of land – does not grow automatically with real income growth or inflation, there must be periodic reassessments to update property values. This is an administrative problem because local governments fall behind in carrying out reassessments owing to lack of suitably qualified staff. Thus, old property values remain on the tax rolls, and revenue losses are substantial.

Another problem is the notoriously low rate of tax collection. Evidence on this is not readily available, since local government records on revenue collection performance are not reliable, and the specific reasons for poor revenue collection performance differ across local authorities. However, common elements can be found, the most important being the absence of effectively
enforced penalty measures for non-payment or unduly delayed payment. Collection problems may stem from inadequacy of staff as well as from the structure of the tax: wide variations in the equity of property tax assessments (i.e., in the ratio of assessed value to market value) are a typical obstacle in this respect.

Another frequently cited problem is that many tax delinquents simply have no capacity to pay. Also, procedures for collection and recovery of late payment/arrears are generally poor. Enforcement is both time-consuming and cumbersome, as follow-up measures are not clearly defined.

Some governments in the continent have begun to deal with these problems with a variety of measures. The most effective one, however, appears to be strict enforcement, including prompt identification of delinquents, rapid legal procedures, and automatic tax liens on delinquent property.

Other forms of taxation, for instance on the use of cars, although well suited to urban areas, have been little used by African countries. Car ownership has increased significantly in most developing countries and is largely concentrated among high-income groups, but taxes on cars do not cover the costs of road networks, parking space, and traffic regulation, let alone generate surplus revenues for the development of urban services. Car taxation has the advantage that it can be made progressive and used to promote public transport, an investment of particular benefit to the poor.

Central governments should encourage local authority efforts to generate income – especially since such actions can enhance equitable income distribution at the local level – and to strengthen local management capabilities. Appropriate methods would include, *inter alia*, incentives to improve local authorities' revenue generation through performance-linked grant systems, and assistance in organizing borrowing from financial institutions. Such support could help secure the capital required for investments in fixed infrastructure as well as reduce the demands for grant and loan funds from central government.

This approach transforms the traditional system of transfers from central to local government, from one of annual handouts covering deficits and centrally planned and funded investments into one of reliably sourced finance for locally planned and managed services and infrastructure.

### 3.4.2 Sub-national government autonomy

For local authorities to succeed, they need autonomy and this means that central governments must decentralize their activities to municipalities. Research shows that Ghana, South Africa, Tanzania and Uganda have maintained the greatest levels of decentralization, as measured by the powers (executive, legislative and judicial) granted to lower levels of government. Zambia has pursued a quasi-decentralization programme in which powers are granted (deconcentrated) to local authorities only in a partial sense (Ludeking and Williams, 1999). In the case of South Africa, decentralization has been introduced as part of the process of constitutional change, with considerable attention to be directed towards the creation of a sound, overall framework of decentralization, including the establishment of autonomous, financially stable governments with the capacity, *inter alia*, to address infrastructure needs.

While South Africa’s overall system is not yet properly bedded down, important elements are in place. National government guarantees of local government debt are illegal, yet there is fairly significant lending by private financial institutions to metropolitan municipal governments in particular. In 2004, the City of Johannesburg successfully floated a general obligation municipal bond, unsecured by any revenue intercept or national government guarantee (van Rynveld, 2005).

On the other hand, there are few countries without serious decentralization of powers and resources. In Kenya, for example, there is some autonomy, but ministerial approval is required for most of the decisions made by councils. In Malawi, Botswana and Rwanda, autonomy has historically been weak due to capacity constraints.

In other instances, local authority efforts are stifled by the centre. For example, efforts to increase council revenues in Harare have been frustrated by the central government through certain requirements, such as:

- City’s proposals to increase rates, charges and fees must be approved by the parent ministry, the Ministry of Local Government;
- These proposals are often turned down, or the increase allowed is too low to make any significant improvement in revenue;
The government has delayed provision of an enabling legislation which will allow the city to charge rates instead of supplementary charges in high-density areas (which continue to enjoy similar services to those paying rates in the medium- and low-density areas) (Kinyungu, 2004).

Governments need to complement decentralization policies with institutional frameworks – legal, financial, and administrative – to enable popular action: decentralization alone does not foster popular participation. Secondly, local authorities can enable community action even if central government is reluctant to devolve administrative authority.

3.4.3 Fiscal Decentralization and Municipal Finance: Slow decentralization

Fiscal decentralization, which can help municipalities finance their social and physical infrastructure programmes, is relatively slow in the African sub-continent and this has posed a challenge to most authorities.

The concept of municipal finance in most developing countries is predicated on the practice of decentralization, and fiscal decentralization in particular, as local governments are almost wholly dependent on the centre for a great part of their recurrent and capital budgets. The last decade has witnessed an extraordinary proliferation of local government reforms around the world, including in Africa. Rapid political, economic and technological changes have fuelled the trend of relying more heavily on lower levels of government. Fiscal decentralization has not accompanied the decentralization of responsibilities. Although the local authorities are increasingly being charged with service and infrastructure provision responsibilities, they still have to revert to the central government for funding. They are still subjected to tendering and asset disposal procedures practiced at central government level. This inevitably does not give local authorities the latitude to deal with their finances and revenue-generating practices as they see fit.

Fiscal decentralization may appear to be the “easiest” aspect of decentralization, because it is not difficult to assign additional powers and revenues to sub-national governments like municipalities. The reality, however, is far more complex. Even if a formal decision is made to decentralize, reluctant central agencies may slow the progress. In addition, giving additional resources to sub-national governments that politically, managerially and technically unprepared to use them responsibly can create enormous problems. Finally, the degree to which fiscal decentralization should be pursued is unclear. Empirical evidence to justify or discredit fiscal decentralization is scant and mixed. None of the claim on either extreme – that fiscal decentralization retards economic development and has undesirable macroeconomic effects; or that it improves local service delivery and enhances local government accountability – has been adequately tested (Ter-Minassian, 1997).

Fiscal decentralization may be more effective if it is approached in an experimental, phased version rather than adopted in one fell swoop. Namibia and Mozambique are starting with the cities while Uganda started with the fiscal component of its decentralization programme in 13 districts. Tanzania did the same in the early 1980s. Nigeria started in 1976 and Ghana in 1991.

A study by Smoke (2001) of four countries in the Eastern Africa sub-region (Ethiopia, Kenya, South Africa and Uganda) gives an insight into local government finance and decentralization. Some key differences are summarized in Table 6. The ratios of public expenditure to GDP for Ethiopia, Kenya, South Africa and Uganda were respectively 29 percent (in 2000), 30.5 percent (1996), 25.3 percent (2000) and 21.9 percent (2000). Their respective deficits in those years were -22.4 percent, -7.5 percent, -2.4 percent and -10.1 percent. Thus, the overall size of the public sector is moderate in all cases. All countries ran deficits, with Ethiopia having the largest and South Africa the smallest.

The relative importance and fiscal independence of decentralized governments vary considerably across the four countries. Ethiopia’s decentralized government (primarily the states) accounted for 31.2 percent of total public expenditures (2000) and raised 18.9 percent of total expenditure revenues, while Kenyan local government accounted for only 4.2 percent of expenditures and 5.6 percent of revenues (1996). In Uganda, local governments accounted for 28 percent of expenditures (2000), but they raised less than eight percent of revenues. South Africa has two sub-national levels of importance. Provincial governments accounted for 46 percent of total expenditures (2000), but they raised an average of only four percent of their revenues, while local governments accounted for 25
percent of public expenditures, but they raised on average 92 percent of their revenues (more in larger urban areas, less in small rural).

Functional responsibilities are quite different in the four cases. In Ethiopia and South Africa, decentralized levels of government (primarily state/provincial) have dominant responsibility for social services (health, education and, in South Africa, welfare). In contrast, only a few large, colonial-era municipalities are involved in health and education in Kenya – social service expenditures are almost entirely funded and provided by the central government and NGOs. In Uganda, local government has significant responsibilities for health and education by law, but in many cases has not been able to deliver these services adequately since decentralisation, due to capacity constraints.

The four countries also have dissimilar local revenue structures. Ethiopian states rely on shared percentages of central taxes (personal income, business, excise, sales) and have only a few modest independent sources, especially enterprise profits and various charges and fees. Kenyan local government has relied heavily since independence on property tax, and since the late 1980s on local authority service charges, a combination payroll and business tax. The LADC was abolished in 2000 and replaced by a transfer system. South African provincial governments' main sources of revenue are motor vehicle fees, gambling revenue and hospital user charges. Local governments rely very heavily on surpluses from trading services (mainly electricity and water), with urban areas also relying on property rates, and large metropolitan councils and districts on the Regional Service Council levy, a productive but problematic combination payroll levy and turnover tax. In Uganda, the most important source of local revenue is the graduated personal tax, an unusual and complex hybrid of PAYE (pay as you earn) income tax, a presumptive income tax, a wealth tax and a poll tax. Local governments have access to the property tax, but in practice, few use it, and it is significant only in the large cities. Sub-national governments in the four countries use various types of fees, licenses and other minor revenues.

Finally, the four countries have significantly varied approaches to intergovernmental transfers, both in terms of relative importance and structure. In Ethiopia there is a single block transfer programme based on a complex formula that accounts for more than 400 percent of the national budget (2000). Kenya for many years had no transfers except for teacher's salary grants to a few municipalities that provide primary education and a very small grant to needy councils. A transfer system to distribute five percent of central income tax revenues to local governments was adopted in fiscal year 2000. South Africa provides provinces and municipalities with an “equitable share” of national resources for recurrent expenditures. This transfer funds more than 95 percent of provincial expenditures, but less than 10 percent of municipal expenditures on average. Provinces and municipalities also have access to a variety of conditional transfers primarily for capital expenditures, some of which are off-budget. Uganda's transfer system is designed to provide three types of grants: block, equalization and conditional.

From the above it can be seen that the level of autonomy, responsibility and power depends on the political set up of the sub-national governments. This shows that local governments do get financed in different forms and amounts depending on the level and scale of fiscal decentralization. Efforts to raise their own funds vary and depend on various factors.

3.4.4 Sub-national Government – Decentralization and Capacity building

One of the major problems that face municipal/local governments is lack of capacity to run projects and programmes in their areas of jurisdiction or to manage revenue and expenditure. UN-HABITAT explains the concept of “capacity” as comprising a combination of knowledge, skills and aptitudes that individuals need to carry out what they consider to be their “mission” in their particular circumstances. Capacity, therefore, is the quality of ‘doing and acting’ as a function of expected aims, proposals and results. Capacity building also means strengthening all the agencies that take part in the implementation of plans and programmes, including legal instruments. Capacity building is a generic concept that is used interchangeably with terms such as institutional strengthening; institutional development and organizational development. Capacity development is preferred by UN-HABITAT, as capacity building implies that there is no capacity at all which is hardly ever the case.
<table>
<thead>
<tr>
<th>Table 6. Local Government Finance: Selected Countries</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Structure of sub-national Government</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>- Provincial</td>
</tr>
<tr>
<td>- Municipal (Type A, B, C)</td>
</tr>
<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>- State</td>
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<tr>
<td>- Administrative tiers of state</td>
</tr>
<tr>
<td>- Municipal</td>
</tr>
<tr>
<td>Kenya</td>
</tr>
<tr>
<td>- Local (Municipal, Town, Urban, County)</td>
</tr>
<tr>
<td>Uganda</td>
</tr>
<tr>
<td>- Local (Districts and four levels below)</td>
</tr>
<tr>
<td><strong>Size of sub-national government</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>Provincial and Municipal</td>
</tr>
<tr>
<td>&gt;60% expenditures</td>
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<tr>
<td>&lt;15% revenues</td>
</tr>
<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>31% expenditure</td>
</tr>
<tr>
<td>19% revenue</td>
</tr>
<tr>
<td>Kenya</td>
</tr>
<tr>
<td>5% expenditure</td>
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<tr>
<td>6% revenue (prior to recent reforms)</td>
</tr>
<tr>
<td>Uganda</td>
</tr>
<tr>
<td>28% expenditure</td>
</tr>
<tr>
<td>8% revenue</td>
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<tr>
<td><strong>Sub-national Government Expenditures</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>Social services (Provincial)</td>
</tr>
<tr>
<td>Local Services (Municipal)</td>
</tr>
<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>Social services, infrastructure</td>
</tr>
<tr>
<td>(state) Local services</td>
</tr>
<tr>
<td>Kenya</td>
</tr>
<tr>
<td>Local services and some infrastructure</td>
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<tr>
<td>Uganda</td>
</tr>
<tr>
<td>Social services.</td>
</tr>
<tr>
<td>Some infrastructure, Local services</td>
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<tr>
<td><strong>Sub-national Revenues</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>Road tax/fees, Gambling (Provincial)</td>
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<tr>
<td>User charges, Property rates and RSC (local)</td>
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<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>Enterprise Tax (state)</td>
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<tr>
<td>Fees/charges</td>
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<tr>
<td>Property tax (urban)</td>
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<tr>
<td>Kenya</td>
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<tr>
<td>Property rates, User charges</td>
</tr>
<tr>
<td>Agricultural cess (rural)</td>
</tr>
<tr>
<td>Uganda</td>
</tr>
<tr>
<td>Graduated personal tax, Property rates, User charges</td>
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<tr>
<td><strong>Inter-governmental tax sharing</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>Provided for provinces, not yet used</td>
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<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>Income, sales, Business, Excise</td>
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<tr>
<td>Kenya</td>
</tr>
<tr>
<td>Income (newly instituted fiscal year 2000)</td>
</tr>
<tr>
<td>Uganda</td>
</tr>
<tr>
<td>None</td>
</tr>
<tr>
<td><strong>Inter-governmental Transfer Programmes</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>Equitable share (formula based distribution of an</td>
</tr>
<tr>
<td>annual ad hoc allocation) Various capital transfer</td>
</tr>
<tr>
<td>programs</td>
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<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>Block transfers (formula-based distribution of the</td>
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<tr>
<td>proceeds of certain taxes)</td>
</tr>
<tr>
<td>Kenya</td>
</tr>
<tr>
<td>Block transfers (formula based distribution of tax</td>
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<tr>
<td>share, but reform conditions placed on a portion.</td>
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<tr>
<td>Uganda</td>
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<tr>
<td>Unconditional, Equalization, Conditional</td>
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<tr>
<td>(separate formula)</td>
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<tr>
<td><strong>Sub-national borrowing</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>Once substantial in metros, then declined, new</td>
</tr>
<tr>
<td>framework in development</td>
</tr>
<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>None, except some at state level for short term</td>
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<tr>
<td>cash flow management</td>
</tr>
<tr>
<td>Kenya</td>
</tr>
<tr>
<td>Once substantial, now virtually gone</td>
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<tr>
<td>Uganda</td>
</tr>
<tr>
<td>None</td>
</tr>
<tr>
<td><strong>Central Government Oversight</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>National Treasury, Departmental of Provincial and</td>
</tr>
<tr>
<td>Local Government</td>
</tr>
<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>PM Office, Ministry of Finance, Ministry of Works</td>
</tr>
<tr>
<td>(Municipal)</td>
</tr>
<tr>
<td>Kenya</td>
</tr>
<tr>
<td>Ministry of Local Government, Ministry of Finance</td>
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<tr>
<td>Uganda</td>
</tr>
<tr>
<td>Ministry of Local Government, Ministry of Finance, Planning and Economic Development</td>
</tr>
<tr>
<td><strong>Sub-national Autonomy</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>Relatively strong legally and in practice</td>
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<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>Strong legally but weak in practice</td>
</tr>
<tr>
<td>Kenya</td>
</tr>
<tr>
<td>Relatively strong but some control</td>
</tr>
<tr>
<td>Uganda</td>
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<tr>
<td>Strong legally, but weaker in practice</td>
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<tr>
<td><strong>Sub-National Government</strong></td>
</tr>
<tr>
<td>South Africa</td>
</tr>
<tr>
<td>Mixed (stronger metropolitan)</td>
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<tr>
<td>Ethiopia</td>
</tr>
<tr>
<td>Weak, but some better than others</td>
</tr>
<tr>
<td>Kenya</td>
</tr>
<tr>
<td>Mixed across urban and rural</td>
</tr>
<tr>
<td>Uganda</td>
</tr>
<tr>
<td>Mixed, generally better in urban</td>
</tr>
</tbody>
</table>

*Source: Snaile (2001)*
Most municipalities do not have the right calibre of both managerial and technical staff to plan and implement projects successfully. Professionals like engineers, architects, and quantity surveyors are hard to come by. Even where countries do have such cadres, the municipal councils cannot employ them, as salaries offered are not attractive enough.

In Kenya, the level of capacity is mixed, although the Kenya Local Government Reform Programme proposed developing capacity to deliver services, plan and implement projects using community-based participatory planning. In Uganda, most decentralization projects that have been undertaken have included capacity-building components. In Nigeria, the situation is highly variable. Lastly, in Malawi, Botswana and Rwanda the system has been weak due to historical central government control.

Examples of some African countries that have recognized decentralization, often to the community level, as one of their primary strategies for development include Uganda, Mali, Burkina Faso, Zambia, Côte d'Ivoire and Zimbabwe.

(a) In Uganda, national policy on decentralization transfers real power to the 39 districts, brings political and administrative control over services to the point where they are actually delivered, frees local managers from central constraints, establishes clear links between payment of taxes and the provision of services they finance, and improves the capacity of local councils to plan, finance and manage the delivery of services to their constituents. In the decentralization process, central government personnel were transferred to the district level. Financial management and administration followed, after ensuring accountability and transparency at lower levels.

(b) A succession of laws in Mali has established the governing bodies for municipalities, counties and regions and sets out the responsibilities of each. Through greater citizen involvement, there has been much innovation at the local level and a remarkable degree of public awareness and understanding of the decentralization programme. The most significant problem has been the scarcity of resources and bureaucratic resistance among central government ministries.

(c) In Burkina Faso, a National Commission for Decentralization has been set up to strengthen democratic and participatory institutions at local level, promote grassroots development and facilitate resource mobilization. Although challenging, the task is made easier because there is a political will to succeed; the process is not being implemented hastily, and there is a strong tradition of public participation in the country.

(d) Zambia, following a government decentralization policy, has established a District Development Fund (DDF) to provide extra budgetary resources for implementation of bottom-up micro-projects intended to develop the social and economic infrastructure of impoverished areas, launch decentralized participatory planning processes and build capacity. Beneficiary communities are expected to contribute at least 25 percent of the project costs in cash or kind.

(e) In Côte d'Ivoire, a series of laws over nearly two decades has established the communes of Abidjan and Bouake and set the framework of municipal responsibility and authority. The establishment of a continuous training and capacity-building process has been supported by the international donor community. The programme includes a funding facility for local government. Now, more explicit transfer of powers needs to be made between the central and local authorities and more resources must be given to the communes in the form of personnel and taxation power for them to manage their own affairs.

(f) In Zimbabwe, the division of powers between the national and local levels, set by an Act of 1985, varies according to the categories of services, activities and functions. Central government focuses on guidelines, national policy, standards enforcement, national planning, financing and the development of infrastructure of national importance. Central government has a supervisory role over local authorities and a facilitating role in negotiating loans for capital development on behalf of a local government; and sometimes in controlling prices charged for services and leases. Mandatory local functions include such services as provision of water and roads, health services, refuse removal, sanitation and drainage services, provision of housing and service standards and planning.

(g) Upon full independence, the government of Eritrea conducted a seminar among all stakeholders to help gain acceptance of a new, decentralized system of
government. The system aimed at achieving balanced development, ensuring popular participation in deciding local affairs, and encouraging local initiatives. Experience, so far, indicates that incentives should be instituted to encourage competent line department staff to work at the lower level units; more attention needs to be paid to the drawing of district boundaries; the shortage of material, financial and human resources must be addressed; and Councillors need to fully understand central government department policies.

(h) In South Africa, central government shares revenue with the local level using a specific formula. For local government, the formula is based on household per capita income and for provinces on household per capita income augmented by a measure of the extent of the rural economy in the region. The system has eliminated ad hoc and inequitable fiscal transfers. Central government has created a mechanism of grant funding for municipalities to expand their ability to buy capacity for projects involving the private sector in the delivery and financing of municipal services.

In sum, capacity building at Local Authority level is needed in order:

1. To build / enhance the requisite ability to respond to emerging challenges in urban governance such as participatory budgeting;
2. To build the necessary confidence to consult with the community in the spirit of promoting partnerships in services delivery;
3. To develop and put in place systems that recognize and promote the values of democracy (see Box 1), transparency, accountability and social equity in all activities undertaken by the Local Authority;
4. To build a sense of inclusiveness where Local Authorities view communities as an asset that requires soft nurturing and
5. Central Government and the community equally require capacity building in order to reinvent their predominant cultures/values.

3.4.5 Mismangement and corruption

Even where formal democratization has been introduced in most municipalities in Africa, the problem of finance has come from poor management of the resources allocated for development and from corrupt practices, which now are a cancer in the continent. Many projects either do not get started at all, or those that are started get stalled due to

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**Box 1: Africa Supports World Charter of Local Self-Government**

In a significant move towards internationally shared principles of local democracy and self-government, representatives of national and municipal governments from Anglophone and Francophone Sub-Saharan Africa and North Africa, as well as representatives of municipal associations from the regions, gave their strong support to the World Charter of Local Self Government at meetings in Accra, Ghana, and Agadir, Morocco. In doing so, they underlined the importance of decentralization in harnessing the creative energy of people for economic growth and development on the continent and to the process of democratization in Africa. Welcoming senior delegates to the Accra consultation in March 2000, the Vice-President of the Republic of Ghana, Professor John Atta-Mills pointed out that “long gone are the days when central governments could decide for all citizens. With the growing population, local governments should be enabled to manage all local affairs. The Charter should constitute a blueprint for local government development in Africa.” At the Agadir regional meeting, held in June 1999, the Moroccan Minister of Regional Planning, Environment, Reconstruction and Housing, Mr. Mohammed El-Asighl, said that his country’s strategy was to “strengthen the decentralization process and to be nearer to the citizens within the framework of partnership with all stakeholders.” A generally shared opinion at the meetings was that decentralization, local autonomy and financial self-reliance were necessary for anchoring democracy in national political life. However, for such policies to be successful it is necessary to design practical measures for effective co-operation between national and local authorities. It was noted, however, that these measures would need to be sensitive to the particular historical, social and economic circumstances of the African region.

*Source: UN-HABITAT, 2003*
funds having been siphoned off by corrupt officials acting alone or in collusion with people in the private sector. In other instances, projects are mismanaged due to lack of managerial skills among council officials.

The 2005 “Corruption Index” shows Botswana as the least corrupt country in Africa (number 32 in the world) followed by South Africa (46), Namibia (47) and Seychelles (55). The most corrupt countries are Chad (158), Nigeria (152), Equatorial Guinea (152) and Kenya (144) (World Transparency International, 2005).

3.4.6 Rising poverty levels
In all African countries, urban as well as rural poverty is growing as a result of declining economic performance, political instability and growing marginalization of the region in the global economy. Until the beginning of the 1980s, poverty was largely rural, but now it has moved to urban areas at high speed, forcing municipal governments to tackle the problem head on. Virtually all local governments have been involved in one way or another in dealing with poverty, through poverty reduction strategies. Such strategies have been prepared in Tanzania, Uganda, Botswana, Kenya, Rwanda, South Africa and many other
countries. However, due to lack of resources, success has been eluding the majority of them. More direct action is needed if this problem is to be stemmed or at least reduced.

3.4.7 Resistance of privatization attempts
Privatisation of the provision of municipal services is one avenue of saving money but the general public resists this approach. Inefficient and economically unfeasible provision of services is where the privatisation debate, sometimes heavily loaded with ideology, comes in. The financial and service delivery records of state-owned enterprises around the world are not particularly impressive, yet the transfer of such services to private ownership is usually an integral part of any structural adjustment programme. Political interference, transferring income to the general fund and packing the staffing rolls with unneeded workers can lead to poor performance and productivity. This reflects the fact that public organizations are often free of the discipline of financing their own operations or responding to market demand. One immediate fallout from privatization is usually the layoff of supernumerary workers with all the social welfare implications that it entails and the lack of access by the poor alluded to above.

3.5 Good Practices: Innovative Practices Adopted for Mobilizing and Managing Municipal Finance

In spite of the challenges cited above, in this section we highlight some of the good practices that we have come across in mobilizing funds for municipal development or better management of funds in various countries in the African region, the objective being that other countries could borrow a leaf from these examples.

It has been documented that many cities and municipalities have improved their collection systems; improved financial management by computerizing their accounting systems or adopted stringent auditing systems; some have introduced public-private partnership; others have engaged in revenue-generating projects, and some have improved billing and revenue collection systems.

3.5.1 Kenya
A study of municipal finance and budgeting in several towns in Kenya by Lewa and Devas (2004) has highlighted the following good practices of municipal finance and governance:

(a) Nyeri Municipal Council – population: 100,000
   - Privatization of water and sewerage, resulting in more efficiency
   - Introduction of an Integrated Financial Management System (IFMS). IFMS has the following elements:
     - revenue management, including taxpayer registers, billing, receipting and accounting,
     - expenditure management, including voucher issuing, payment cheque issuing and accounting,
     - budget preparation and monitoring
   - accounting
   - Citizen participation and consultation in Council matters.
   - Resource augmentation

(b) Maragua Town Council – population: 20,000.
   - Simplified accounting system for the preparation of accounts
   - Introduction of a Single Business Permit which serves the population promptly.

(c) Mavoko town, with a population of 30,000:
   - Introduction of an integrated financial information system; involvement of stakeholders in project selection and neighbourhood meetings; implementation of the Single Business Permit, and other revenue improvements.

3.5.2 Mozambique
Areas where some local governments have made strides in addressing local finances, and particularly with relation to raising more resources locally, have been: computerisation for record-keeping (although sadly many computers are out of operation due to viruses and power surges) and high-profile moves against defaulters who are often public entities (army, police, etc.) or elites/businessmen. By exposing such defaulters, popular opinion can go a long way towards persuading people to pay local rates/taxes. Budget information is also freely available. Disseminating information about the budget is important; public events to explain budget priorities and public posting of the budget are all small steps that help increase transparency.
and encourage dialogue between local government officials and civil society. In this area of information flow, the local media have a very important role in encouraging more openness from local government.

3.5.3 Botswana
Some of the good practices adopted in the municipalities include:
- Public-private partnerships in land servicing,
- Cross-subsidies in land pricing for residential areas
- Attempts at property tax arrears collection through “Name and Shame” action programme and the use of private loan collector.
- Computerization of Council accounts, rates and land management since 1999.

3.5.4 Zimbabwe
Urban local authorities, in particular, have introduced many innovations to increase local revenue, including:
1. Improving billing and revenue collection systems. 22 local authorities are using a standard computerised system. This has helped improve efficiency in monthly collections;
2. Many local authorities have partnerships with private organisations in:
   - Revenue-generating businesses;
   - Service delivery, including water and waste disposal;
   - Infrastructure development;
   - Housing development;
3. Raising finance from the market by issuing municipal stocks and other innovative financing mechanisms;
4. Income-generating projects that contribute up to 26 percent of revenues for the larger cities. The projects include brewing and selling beer, abattoirs, brick manufacturing, and factory shell rentals;
5. Innovations also include the way services are priced in relation to consumers’ incomes;
6. It is estimated that urban local authorities contribute about 15 percent of GDP (1996). An interesting observation is that the cities in Zimbabwe are able to recruit and retain highly skilled and experienced staff due to their relative autonomy to hire and reward. The accounting system is functional with relatively good controls and mandatory audited accounts. The budget is prepared by committees with limited input by the communities. Issues of urban poverty are handled indirectly in the budgets through the pricing of services and subsidisation. NGOs seem to have clearer programmes and budgets for poverty reduction and, in some cases, work with local authorities in this area. It is a requirement, however, that before budgets are sent to central government for approval, new tariffs are advertised and community consultations be held to explain and get inputs into the budget. The executive mayor is required to sign a certificate of consultation as proof that the consultations were made.
It is rather sad that despite all the efforts that have been made over the years to improve local governance, poverty has been rising in the urban areas of Zimbabwe. Maybe it could have been worse without these efforts.

4. Conclusion

From the foregoing and as amply demonstrated by various practices in many African cities and municipal governments, raising revenues from “own sources” is a mammoth task. As a result, many local authorities depend on central government transfers and sharing of resources to provide services. Municipal governments that want to achieve revenue autonomy face severe constraints in choosing their fiscal patterns. Even when they have had substantial freedom of action, their existing revenue authority has not always been fully utilized. The revenue instruments that seem most underutilized are property taxation,betterment levies, and user charges. Thus, the degree to which a city’s government is able to meet its rapidly rising expenditure requirements depends only in part on its revenue capacity as determined mainly by the economic base of the city and by the restraints imposed by higher-level governments. It also depends on revenue effort, that is, the extent to which the local government is using its revenue capacity.

In short urban local government revenues in many African states are generally not enough to develop and provide adequate urban services to the region’s fast growing urban populations. This is reflected in the poor physical state and operational inefficiencies characterizing many of the services, especially water and sanitation, waste management, roads and education, as well as in the
low levels of access to these basic services. Most cities have chronic budget deficits.

It is also apparent that, while there is a need for greater sharing of revenue sources between central and local government, the yield potential of the sources currently available to local authorities is far from being fully exploited. Thus, significant results could be achieved through improvements in collection from currently available revenue sources, especially property rates, business licenses and service charges. If this is to be achieved, improvement of data on revenue sources and payers is a major imperative, especially with respect to the ubiquitous informal sector. It is worth noting, however, that some positive and interesting developments have been noted in the African region, including privatisation of revenue collection.

4.1 The Way Forward: Strategies for Mobilizing Municipal Finance and Financial Management

As seen in the review above, in most African cities, basic infrastructure and services are already stretched beyond capacity. This means that economic growth is being stunted, quality of life is spiralling downward and urban poverty is on the rise. Now consider that urban population in the continent is projected to double in the next 20 to 30 years. This explosion in urban growth compounds the need for expanded basic services to the urban poor and improved infrastructure that attracts businesses and strengthens a city's competitiveness. The management and financing of these needs will increasingly become the responsibility of city governments as more and more countries decentralize fiscal and administrative functions. Thus, city governments have a substantive role in financing capital improvements and facilitating local investment through the mechanisms available to them, including local revenue generation through tax and fee collection, public-private partnerships, equity sharing of capital projects, and tapping debt markets.

We have seen how various countries have sought to mobilize municipal finances, with some successes here and there.

Possible future strategies that can be adopted are organized along the following lines of action:

- Creating and enabling environment,
- The creditworthiness of Cities
- Proper planning
- Identification of bankable projects
- Finance mechanisms
- Commercialisation and privatisation of urban infrastructure
- Mobilization of community resources
- Value for money in the use of funds by sector agencies.

4.1.1 Enabling Environment

An enabling environment at the national level can help a city government to finance basic services and infrastructure. Central government should decentralize predictable revenues to cities — through a broad tax base and stable transfers — and make it legal for cities to use their land or other assets as collateral. Legislation should allow for direct private sector investment in public services through leasing and concession arrangements that allow the investor to reap appropriate benefits from the investment. In countries where cities are still gaining experience with borrowing, national guidelines for limiting borrowing or for maximum debt service levels, for example in relation to their budget, may be appropriate. A legal framework and predictable enforcement thereof — at the national and local levels — also contribute to an enabling environment where city authorities are empowered to manage their service and infrastructure needs and the attendant financing.

Central and local governments should be aware that investors, lenders, and credit agencies consider the following factors as indicators of high risk, and should take actions to reduce them:

- Newly created and evolving legal frameworks;
- Shifting intergovernmental relationships;
- Incomplete or outdated demographic and socio-economic data;
- Financial data that is not independently audited or prepared according to international standards;
- Risky debt profiles (short-term; bullet maturity; foreign currency exposure, etc.);
- High levels of contingent liabilities (for example, numerous and weak municipally owned companies, large number of guarantees issued by municipalities, and unfunded pension liabilities); and
High levels of uncollected taxes and fees.

4.1.2 The Creditworthiness of the City
Creditworthiness is important to cities interested in financing capital improvements because it is a determining factor which investors and banks use to assess risk. To encourage private sector investment, city governments should take steps to increase transparency and reduce corruption at the city level. City governments can use performance-based budgeting, independent audits of city finances and double-entry accounting to demonstrate consistent governance despite fluctuations in political leadership. City governments should also develop and follow a capital investment plan that identifies and appropriately sequences priority investments and takes into account the reduced operating and maintenance costs/savings deriving from such capital investments. In cities interested in a general-purpose loan collateralized by the city’s general revenues and a pledge to use a share of the revenues for loan repayment, the city government should efficiently administer its taxes, have stable revenues and build a solid record of loan repayment. Without these conditions, investors are more likely to require collateral in the form of physical assets.

4.1.3 Planning
Ensuring customer satisfaction with capital investments begins with a participatory and transparent planning process. City leaders should invite citizens (future customers), and stakeholders from the business and NGO sectors to identify their priorities and expectations for municipal capital investments as well as their willingness to pay for new and improved services. The service and infrastructure priorities identified by the community and their willingness to pay should drive local government decision-making. City leaders should also manage expected future growth by linking financing initiatives, such as the city’s capital investment plan, to broader urban planning and community visioning exercises. Given the projected rate of urban growth in the African continent, it is essential that city leaders be forward-thinking in planning their service and infrastructure improvements. Inviting participation from citizens, particularly the urban poor, can include engagement in city planning through referenda, public comments on zoning and land use decisions, and public hearings on the budget or the city’s strategic plan.

4.1.4 Identification of Bankable Projects
Identifying infrastructure priorities through participatory planning and growth management and establishing the city’s creditworthiness may not be enough to entice local private investment. City governments will also need to identify those city investment projects that are bankable (i.e., projects in which the private sector would want to invest). Investors judge the creditworthiness of individual projects based on financial analyses that include past, present and projected municipal revenue streams, sources and uses of project funds, debt service schedules and project revenue schedules. Investors will also assess the efficiency with which the relevant enterprise is currently managed, the capacity of its staff and the costs to operate and maintain the facility once completed. Investors – both equity shareholders and lenders – may perform additional project analyses to determine other risks associated with project (investment) viability, including probability of service delays and shutdowns and their likely effects on demand. City governments can identify bankable projects through access to: demographic and socio-economic statistics about customers, history of predictable revenue generation, reliable mechanism for revenue collection, and projections for future growth prospects and profitability.

4.1.5 Finance Mechanisms
Mechanisms for financing local capital investment needs range from the city’s operating budget and expansion of local revenue through better tax and fee collection, computerizing the accounting system, better financial management, as well as public-private partnerships such as leases, concessions, and in some cases actual privatization.

As a rule, funds should be channelled to municipalities/cities or to the lower levels at which implementation takes place. Capital grants for community projects should follow the most direct route from the source to the communities.

Revenues from property tax can be improved by many actions, including (a) carrying out valuations more frequently (b) follow up defaulters more vigorously (c) simplifying administrative procedures and (d) review property rates annually.

Enhancing Resource Allocation to Urban Development in Africa
As far as *income tax* is concerned, the following is proposed: (a) The access of local authorities to a larger share of national taxes, including income tax, could be improved, (b) introduce graduated rates of tax, (c) need to improve city-wide enterprise and employee databases in order to ensure that employers remit to government all contributions collected from their employees and that all eligible employees pay their dues. Ways also have to be found of ensuring payment by informal sector employees and enterprises.

Municipal service *user charges:* The following is proposed - (a) Clearly-defined systems of charging for all services provided by urban local authorities should be put in place to ensure adequate provision, operation and maintenance of the services. Such issues must be clear on key issues such as cost-recovery (full or partial) and subsidization of poor communities, (b) In order to overcome a growing feeling of despondency and resistance against paying municipal taxes and charges, local authorities should strive to ensure that services for which citizens pay are adequately provided, efficiently operated and effectively maintained. Ways have to be found of dramatically improving the service delivery capacity of urban local authorities, (c) Market rents should be charged for houses owned by municipal local authorities, (d) Clearer and equitable policies on cost-sharing in the area of education and health should be worked out, ensuring improvement of quality in the provision of these services and guaranteeing universal access, (e) Privatisation efforts should be intensified in order to improve efficiency in the provision of services, yet at the same time ensuring that the poor are not excluded in terms of access to those services.

Tax on provision of goods and services (*business license fees*): As a source with a lot of potential, greater effort should be put into thinking about ways of maximizing the yield from such fees, including clearer and fairer sharing of the source between central and local governments. Also, ways must be found of ensuring compliance by the many business enterprises operating in the informal sector.

As for *borrowing,* (a) Governments should consider resuscitating local authority loan bodies; (b) public-private sector partnership avenues could also be explored in order to identify and put in place more sustainable local authority loan sources; (c) borrowing is considered necessary as a source of revenue, specific provisions should be tailor-made for individual cities, and these must be based on their level of creditworthiness.

In addition, clear and consistent systems of central allocations to local authorities should be put in place, with transparent allocation formulae and timely disbursement; sharing a wide range of taxes is another avenue through which resources accruing to the central government could be allocated to municipal local authorities.

Cities may also draw on other debt financing mechanisms, such as project finance, pooled finance mechanisms, special-purpose authorities, municipal bonds, private sector loans and partial guarantees. Project finance for a municipality is funded by loans that are repaid from the project's revenues, i.e. user fees or tariffs, which are managed in a separate fund. This financing arrangement usually includes a grace period that postpones repayment until the project is completed and project revenues can be collected.

For small to medium-sized municipalities, tapping independently into the local capital market may be difficult because of high transaction costs relative to capital needs. For these cities - and those with infrastructure needs that extend beyond their municipal boundaries - pooled finance mechanisms or bond banks, offer several advantages. Because capital is raised for a group of cities and various investments, the risk to investors - therefore the interest rate for the cities - is lower. Marketing costs are incurred for the fund as a whole rather for individual investments. Such mechanisms also achieve economies of scale in loan origination and supervision.

Another available finance mechanism is the creation of *special-purpose authorities,* which manage a particular government function and are authorized to borrow for investment purposes, subject to constituent approval. Special-purpose authorities have an advantage in that constituents can be confident that the funds raised will be used exclusively for investments related to the particular function. Cities may establish special-purpose authorities within their boundaries or in cooperation with other neighbouring cities. Some examples of areas where special-purpose entities have been successful are common property resources, such as water supplies, wood stocks, fisheries, and transportation infrastructure such as waterways, ports and highways.
For countries with more developed economies such as South Africa, where cities can have identified bankable projects and are in need of longer-term capital, municipal bonds or commercial loans may be appropriate finance vehicles. Municipal bonds pay for such things as bridges, roads, etc., and are secured by a pledge of gross revenues, making payment of debt service senior to payment of operating expenses. Revenues include any income derived from the operation of the project including toll revenues, insurance proceeds, condemnation awards, liquidated damages, and investment earnings as well as any other monies deposited into the revenue fund. Commercial loans are an option cities can pursue for longer-term capital needs.

When the local private sector is reluctant to invest despite an enabling environment, improved city governance and available bankable projects, then international donors could facilitate investment through risk-sharing in the form of partial local currency guarantees, such as USAID’s Development Credit Authority, or the Cities Alliance’s Community-Led Infrastructure Finance Facility and Community Water and Sanitation Facility. In addition to facilitating private sector financing of public capital improvements, donors can help move local firms down market to service the growing number of urban poor by explicitly incorporating low-income neighbourhoods into partial guarantee arrangements.

4.1.6 Commercialisation and Privatisation of Urban Infrastructure

As seen earlier, many African countries are seeking to improve services and facilitate financing of infrastructure by involving the private sector in service provision. In order to measure up to their potential, public-private partnerships must be developed under a framework that ensures accountability, protects the interests of the public, and supports improvement of services to the poor. The latter would have to recognize the role of the “other private sector”, made up of small-scale independent providers (SSIP).

Commercialising and privatising urban infrastructure can involve the following:

Promotion of innovative user-pay instruments:

- Water supply sector: advance registration charges, water benefit/water tax, betterment charges, development charges, octroi, property tax, sale of plots and charges from water kiosks.
- Sewerage sector: connection charges, sewerage cess/tax, conservancy tax, and sale of renewable waste, sludge and nutrient-rich water.
- Solid waste management sector: collection charges, cess, sale of renewable waste, generation of power, fine for dumping waste.
- Transportation sector: Toll tax, use of land as a resource, advertising to generate resource. Surcharge on tickets, toll tax, user charges, and development above and around the terminal, advertising rights.

In addition, initiatives for private sector participation should also be introduced.

4.1.7 Mobilize Community Resources

Poor communities can and do pay for services that they trust and value. Communities, households (in particular women) and small independent operators save, borrow and invest for better services. Sector policies should provide an enabling environment to foster their initiatives.

Central government should collaborate with various agencies and institutions to improve upon various financial mechanisms that facilitate low-income resident access to commercial credits. Governments should scale up such innovative forms of saving (e.g. mutual deposits) and collateral (e.g. collective assets). Where the political commitment is forthcoming, governments should advocate partnerships between the financial service industry and state institutions to guarantee loans of commercial banks to community groups. Alternatively, the various governments should promote community self-financing systems, broad-based savings mobilization through federated community organizations, and public/popular co-financing arrangements.

Investment in social capital and technical assistance is essential to support community and household initiatives, in particular to:

- Facilitate the formation of local partnerships,
- Expose communities to innovation and good practice and link them with networks,
- Provide information on, and access to, formal subsidies and support programmes, and
Ensure necessary linkages with trunk systems, and negotiate support from local authorities and sector agencies (Water Policy International 2000).

4.1.8 Value for Money in the use of funds by sector agencies

Communities should be fully responsible for operations and maintenance of their infrastructure systems. Subsidies for O&M outlays should be phased out and be re-directed to capital expenditure, especially for rehabilitation. In any case, existing subsidies should be kept limited to the level of services affordable by government and consumers.

While the financial principles incorporated in sector policies are generally sound, they are rarely carried into implementation strategies. Guidelines applicable to all actors are needed to define access criteria and rules for the channelling of funds (e.g. through water, sanitation and shelter programme implementation manuals).

The budget framework of central sector agencies needs to be aligned with their new (and more focused) role (e.g. policies and guidelines, programme development and monitoring, oversight of local authorities as well as technical support capacity-building). Staff overloads resulting from the transfer of responsibilities and devolution of functions have to be dealt with. Likewise, resources/assets held by central sector agencies should follow the transfer of functions to local authorities and to communities.

Sector agencies should pursue improvements in management systems and budget controls, and undertake regular audits to enhance their efficiency and accountability. Efforts to reduce waste and to drive out corruption should apply to the sector.
References


Financing of Infrastructure in African Cities by the Private Sector
Mr. Wafula Nabutola, Chairman, Nairobi Central Business District Association (NCBDA)

1. Introduction

Cities and towns are the focal points and drivers of societal development in all countries. At the same time, they are the largest consumers of natural resources and the biggest sources of pollution and greenhouse gas emissions on the planet.

Fortunately, cities and towns also house the greatest concentration of the world’s brains, brawn, money, talent, ambition and vision – all of which need to be deployed to find environmentally and financially sustainable solutions to urban problems.

Cities and towns continue to be seen as offering economic opportunities superior to what can be realized in the countryside. Urban migration takes place on such a scale that we now have a new category of cities – megacities, with populations over 10 million.

Urbanization, population growth, and globalization combine to create vast conurbations of millions of poor people in relatively constrained spaces, with wants and needs basic to all of humankind, yet influenced in particular by the consumption and transportation patterns of Western nations. This is not a recipe for a socially or environmentally sustainable society.

In recent years, suggestions for reforming the provision and financing of infrastructure services in developing countries have focused on private sector participation. This alternative to public financing is seen as a way both to minimize the inefficiencies of public administration and to avoid the need for external borrowing.

Because of the difficulties of assessing projects, investors were reluctant to commit their funds, and governments turned to subsidies and loan guarantees to encourage investment. Often, however, government intervention only replaced one set of problems with another. Investors with government-guaranteed loans had no incentive to monitor the firm’s performance – a limitation that led to the diversion of funds and frustrated the public interest.

2. Service Delivery

Service delivery is the cornerstone of city governance and includes access to water, refuse collection, solid waste disposal, wastewater collection and treatment, and electricity connection. The reliability, quality and cost-efficiency of equitable services to all areas of a city – wealthy and poor – is the primary responsibility of local government, and is the most tangible result for which the community will hold their elected officials accountable.

Fundamental to sustainable and responsive service provision are cost recovery, participatory management, and cooperation to assess needs and ability to pay. Other important factors include (a) accountability and transparency, (b) the creation of an enabling environment for service delivery and (c) efforts to increase coverage to the urban poor.

2.1 Accountability and transparency

Accountability often refers to the relationship between city officials and their constituents, but it also includes the relationship between contractors and city governments, citizens and service providers, and city governments and other levels of government.

Tools for improving accountability include: (i) efficiency measures that compare output produced or outcomes accomplished to inputs provided; (ii) the use of contractors for service delivery, which makes it easier to develop efficiency measures as costs are clearly defined; and (iii) performance benchmarks that help detect problems and build confidence by tracking improvements over time.

2.2 Enabling Environment for Service Delivery

Effective decentralization enables cities better to manage service delivery by giving them the autonomy to (i) set tariffs and user-fees; (ii) determine the appropriate mix and level of services; and (iii) design efficient delivery methods, including the involvement of the private sector.

Other conditions promoting better management of service delivery by cities include:
3. Methods of Service Delivery

3.1 Rationale for Private Sector Financing

- Increasing public demand for higher levels of infrastructure services
- Insufficient public funds; attention has refocused on private sector financing for public projects to restore, rehabilitate, expand or replace existing infrastructure
- Closing the gap in service provision among the poor and the wealthy
- Over 1.1 billion people in the world lack adequate access to safe water
- Nearly 2.5 billion people lack access to sanitation services
- Reduce inefficiencies of public administration
- Avoid the need for external borrowing

For most services, the private and NGO sectors – including user groups and citizen associations – offer the benefits of experience, technology and skill.

The level of private sector involvement should be determined by examining the sophistication and competitiveness of the private sector and the city's own needs for investment and technical capacity.

3.2 Mechanisms for involving the private sector

Contracting out for services when the ends are more important than the means. If private firms (and NGOs) compete to deliver services and are rewarded appropriately for the results delivered, they are motivated to devise cost-saving technologies.

Corporatization when government wants the technical expertise of the private sector to improve management, but wants to maintain overall responsibility.

Leasing and concessions when the government is looking for the private sector to take on more financial responsibilities and risks. Usually, this means a longer-term commitment, from five to 15 years for leases and 15 to 20 years for concessions.

Privatization when the market is well developed and the regulatory framework can ensure that fair pricing and adequate levels of coverage will be maintained.
<table>
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<th>Traditional Public Contracting</th>
<th>Service/Management Contracts</th>
<th>Lease Contracts</th>
<th>BOO, BOOT or BOT Schemes</th>
<th>Concession or Franchise Agreements</th>
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<td>Public</td>
<td>Private</td>
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<td>Public and Private</td>
<td>Private</td>
</tr>
<tr>
<td>Market (Revenue)</td>
<td>Public</td>
<td>Public</td>
<td>Private</td>
<td>Shared (guaranteed minimum custom)</td>
<td>Private</td>
<td>Public and Private</td>
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<tr>
<td>Non-commercial Risks</td>
<td>Public</td>
<td>Public</td>
<td>Public</td>
<td>Public</td>
<td>Public</td>
<td>Joint</td>
<td>Private</td>
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</tr>
<tr>
<td>Sectors where Most Appropriate</td>
<td>Public</td>
<td>Public</td>
<td>Low willingness to pay</td>
<td>Where limited capacity expansion required</td>
<td>Where new facilities are required (e.g. toll roads)</td>
<td>Networked based infrastructure (e.g. water)</td>
<td>Where private capital is required immediately</td>
<td>Where competitive structures can be unbundled</td>
</tr>
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</table>
Those cities selecting to involve the private sector in service provision should be explicit about expanding coverage to the urban poor, particularly in unserviced areas. City governments can facilitate better basic services for the poor through specified deliverables and risk sharing, i.e., partial guaranteed lending. A detailed breakdown of the major characteristics of private sector involvement in infrastructure delivery is provided in Table 1.

3.3 Metropolitan and Community-Based Services

Service delivery can be managed at levels either above or below city government. Cities may find it economical to cooperate on delivering services that naturally extend beyond their borders or when economies of scale or complementarities exist. An example of metropolitan cooperation is the management of supply and distribution of water in the Hyderabad, India metropolitan area.

In the other direction, service delivery can be effective at the community level by empowering user groups and citizen associations to develop effective solutions to their communities’ needs. The involvement of citizens as owners and operators may offer savings as the residents may be more careful to ensure proper maintenance of capital they have bought themselves. Researchers have found that community-built sewerage systems cost approximately one-half to one-third of the costs of systems built by governments. Condominiums are shown to have improved collection rates, as citizens police themselves in the payment of fees.

4. Private Sector Involvement in Infrastructure Development

4.1 Public-Private Partnerships

Any collaboration between public bodies, such as local authorities or central government, and private companies is referred to as a public-private partnership (PPP).

The wide-ranging benefits that the private sector can derive from expanded and improved infrastructure facilities justify the priority accorded to financing infrastructure projects.

4.2 Areas where governments could encourage private sector investment in infrastructure

- Water: bulk water supply, water distribution, sewerage treatment;
- Public housing and social infrastructure, notably health and education;
- Energy and power: power generation, transmission, distribution, renewable energy;
- Oil and gas: pipelines, terminal distribution systems, field development;
- Transportation: roads, bridges, ports, airports, rail transport systems;
- Media and telecommunications: backbone networks, rural telephone systems;

4.2.1 Water, sewerage and environment

To improve living standards and greatly reduce healthcare costs in the long term, clean water and a clean environment are needed. Moreover, water supply is vital to both public health and the manufacturing sector. Due to the necessity of these services, governments must find ways to fund the balance when the full charge cannot be passed on to consumers.

4.2.2 Public housing and social infrastructure

To encourage private sector participation in public housing, governments must recognize that foreign investors require an adequate return on investment. Governments could encourage investment in public housing in a number of ways, for example:

(i) Tax credits: In the United States, tax credits are provided to private developers of low-cost housing.

(ii) Land: In Hong Kong, where approximately 50 percent of residents live in public housing, the government allocates land for community and public housing uses by grants at zero or nominal rent, thereby ensuring that the cost of public housing is 20 to 40 percent lower than private housing.

(iii) Rental/sales: To ensure adequate returns, rental and sales prices must be set at market rates. However, financial assistance could be provided to families on a monthly basis and reduced over time in the case of rentals, and...
in the form of long-term low interest loans to promote home ownership.

4.2.3 Energy, transportation and telecommunications

As they generate sufficiently high-income streams to support returns on foreign investment, these areas attract private sector participation. For example, by locking in long-term (typically 30 years) pre-agreed rates with the developer, the government distribution agency has the opportunity to obtain a premium as the prices to consumers increase over time. Electricity generation and telecommunications projects need to be coordinated with building a rational, cross-border transmission network to meet demand.

Transportation projects require heavy up-front investment and have low-income streams in the early years of operation before traffic and passenger usage grow. Where rates of return fall below the expected norm, governments must actively support the private sector in developing infrastructure. Examples of how governments could assist private developers are as follows:

- Acquiring the right of way and clearing land for developers (which require strong public domain laws);
- Offering non-discriminatory tax holidays;
- Granting additional land to developers at or below market price as an additional source of repayment for the project;
- Providing grants or low-interest long-term loans to projects;
- Offering minimum traffic guarantees or shadow toll rate structures.

4.3 Project Finance

An important characteristic of project finance is that the lenders finance the project based on its creditworthiness, not the creditworthiness of the borrowing party. Repayment of the loans is made from the earnings of the project. Project financing is also known as "limited recourse" financing, as the borrower has limited liability. The security taken by the lenders is largely confined to the project assets.

4.3.1 Build, Operate, and Transfer (BOT) Projects

BOT is a relatively new approach to infrastructure development, which enables direct private sector investment in large-scale infrastructure projects.

The theory of BOT is as follows:

- Build – a private company (or consortium) agrees with a government to invest in a public infrastructure project. The company then secures its own financing to construct the project.
- Operate – the private developer then owns, maintains, and manages the facility for an agreed concession period and recoups their investment through charges or tolls.
- Transfer – After the concessionary period, the company transfers ownership and operation of the facility to the government or relevant state authority.

There are a number of major parties to any BOT project and all of them have particular reasons to be involved in the project. The contractual arrangements between those parties, and the allocation of risks, can be complex.

The major parties to a BOT project will usually include:

(i) Government Agency

A government department or statutory authority is a pivotal party. It will (i) grant the sponsor the "concession", that is the right to build, own and operate the facility; (ii) grant a long-term lease of or sell the site to the sponsor; and (iii) often acquire most or all of the service provided by the facility. The government's cooperation is critical in large projects. It may be required to assist in obtaining the necessary approvals, authorizations and consents for the construction and operation of the project. It may also be required to provide comfort that the agency acquiring services from the facility will be in a position to honour its financial obligations. The government agency is normally the primary party. It will initiate the project, conduct the tendering process and evaluate the tenders. It will grant the sponsor the concession, and where necessary, the off-take agreement.

(ii) Sponsor

The sponsor is the party, usually a consortium of interested groups (typically including a construction group, an operator, a financing institution, and other various groups) that, in response to the invitation by the Government Department, prepares the proposal to

Enhancing Resource Allocation to Urban Development in Africa
construct, operate, and finance the particular project. The sponsor may take the form of a company, a partnership, a limited partnership, a unit trust or an unincorporated joint venture.

(iii) Construction Contractor
The construction company may also be one of the sponsors. It will assume construction and completion risks, that is, the risk of completing the project on time, within budget and to specifications.

(iv) Operation and Maintenance Contractor
The operator will be expected to sign a long-term contract with the sponsor for the operation and maintenance of the facility. Again, the operator may also inject equity into the project.

(v) Financiers
In a large project there is likely to be a syndicate of banks providing the debt funds to the sponsor. The banks will require a first security over the infrastructure created. The same or different banks will often provide a standby loan facility for any cost overruns not covered by the construction contract.

(vi) Other Parties
Other parties such as insurers, equipment suppliers and engineering and design consultants will also be involved. Most of the parties will involve their lawyers and financial and tax advisers.

4.3.2 Indirect Infrastructure Financing
Indirect private sector involvement in infrastructure financing assumes commercial viability. More importantly, it relies on the minimal risk of default on private funds due to the effective ‘guarantee’ on local government borrowings. Indirect private sector financing usually takes the form of local government revenue/infrastructure bonds or debentures. They are issued in the capital markets, usually via a state-underwritten borrowing authority and operate as typical debt instruments.

4.3.3 Direct Infrastructure Financing
The private sector can and has also become more directly involved in the provision of local government infrastructure. Such involvement revolves around the rights and obligations in the contractual arrangements between private operators and Councils and can take the form of service/management contracts, lease contracts, build-operate and invest arrangements (e.g. BOOT, BOO or BOT schemes), concession or franchise agreements, joint ventures or full privatisation.

Each type of direct private sector involvement in local government infrastructure assumes some element of risk and, as with all efficient investment of resources, the ‘risks’ must be adequately counter-balanced by ‘returns’. In terms of local government infrastructure investment, these risks can be categorised as being either:

(i) Commercial risks: cost overruns in construction (construction risks), operation (operational risk) or uncertainties surrounding the demand for infrastructure services (market risk), amongst others; or

(ii) Non-commercial risks: (specifically policy risks), which cover any adverse conditions that are imposed on infrastructure operation because of changes in the regulatory, legal or economic policy framework.

4.4 Risk Structure in Project Finance
Most project finance structures are complex. The risks in the project are spread amongst the various parties; the party that can most efficiently and cost-effectively control or handle it, usually assumes each risk.

Once the project’s risks are identified, the likelihood of their occurrence assessed and their impact on the project determined, the sponsor must allocate those risks. The options are:
(i) To absorb the risk;
(ii) To lay off the risk with third parties, such as insurers;
(iii) To allocate the risk among contractors and lenders.

Apart from the allocation of risks between the private sector and councils, the various forms of involvement can be distinguished by the ownership of the infrastructure assets, capital and recurrent investment responsibilities, basis for remuneration and contract duration.

These differentiating factors can be used to describe the various forms of private sector involvement common in the delivery of local government infrastructure. Prior to this process, it is useful to consider the intensity of private sector involvement via a continuum of responsibility, ranging from full public sector responsibility to full privatisation.
5. Challenges and Opportunities for East Africa

In recent years, suggestions for reforming the provision and financing of infrastructure services in developing countries have focused on private sector participation. This alternative to public financing is seen as a way both to minimize the inefficiencies of public administration and to avoid the need for external borrowing.

Rapid economic growth and urbanization have dramatically increased the demands on the region's already inadequate infrastructure. It is thus becoming increasingly clear that the public sector alone cannot bear the burden of supplying, managing and maintaining the infrastructure to meet the region's growing demand, and that private capital, technology and management know-how are needed.

There is, however, an urgent need for a set of transparent guidelines for governments to facilitate private sector participation and enhance risk mitigation measures in infrastructure development projects in the region. In the formulation and implementation of such guidelines, governments might consider taking the following measures:

(i) Intensify coordination amongst East African economies and between export credit agencies of each economy to help finance infrastructure projects. Member economies should consider ways to promote coordination of their export and investment insurance policies;

(ii) Cooperate with multilateral institutions to further enhance risk mitigation;

(iii) Provide export and investment insurance adapted from successfully executed models, such as those used by Japan's Ministry of International Trade and Industry and the United States' Overseas Private Investment Corporation, as the basis for a carefully structured insurance system;

(iv) Maintain a stable policy and macroeconomic environment and guarantee foreign exchange convertibility. Continuity of policies even with changes in government and administrations is an important consideration for investors;

(v) Ensure that the projects are in accordance with clearly defined domestic development plans and programs that enjoy strong administrative and political support, against the background of clear policies and well-defined means of coordination between government agencies;

(vi) Ensure maximum flexibility in the use of public sector funds and coordination with private sector funding. An example of such coordination would be the case of an electrical power project, where the project itself is carried out under a BOT scheme while related projects such as roads and ports are built with government financing;

(vii) Promote a competition-driven environment for private sector infrastructure projects and open non-discriminatory access to infrastructure. An example would be access to public telecommunications networks for all information providers and users;

(viii) Secure appropriate and responsible risk allocation between the host government and private enterprises;

(ix) Establish and harmonize domestic laws and regulations regarding private infrastructure projects to guarantee currency conversion, policy consistency in setting basic terms and conditions, and fulfillment of government obligations by pertinent authorities at all levels. For example, the Philippines' BOT law of 1990 provides a regulatory and legal framework for infrastructure development that facilitates the entry of private firms in infrastructure projects. In 1994, the law was amended to further improve the environment for private investors; and

(x) Host governments should consider assigning a project manager responsible for interacting with the private investor on all government matters and managing all intra-governmental coordination, to provide the investor with "one-stop shopping" and expedite procedures for approving privately financed infrastructure projects.
Incentives and Support to the Development of the Informal Sector in African Cities
by Paul Okunlola, Assistant Editor, The Guardian Newspaper, Lagos, Nigeria

1. Introduction

Few factors have had such encompassing influence on the characteristics and liveability rating of cities around the world over the past decade as the twin phenomena of globalization and urbanization. The United Nations Human Settlements Programme’s (UN-HABITAT) flagship publication, State of the World’s Cities 2004/2005, states that recent globalization trends have not only significantly impacted the economies of nations, they have also determined changes affecting the social, political, spatial and demographic aspects of cities.

Indeed, with urban-based economic activities accounting for not less than 50 percent of gross domestic product (GDP) in most countries, the relationships between globalization, urbanization and economic growth of cities have been found to be mutually reinforcing.

However, previous assumptions about the economies of urban agglomerations having a multiplier effect and leading to greater returns on investment for individuals, households, firms, production sectors and cities, have not necessarily been borne out in Sub-Saharan Africa (SSA). In fact, in several emerging cases, urban liveability was deemed to have fallen short of metropolitan expectations.

Hence, in the discussion on metropolization, the State of the World’s Cities 2004/2005 report describes urbanization in the region as ‘exceptional,’ in the sense that it is occurring largely without the industrial and economic growth typically associated with the phenomenon in other regions. In other words, the report declares, the prevalent scenario found in Sub-Saharan Africa today, is that of “a region facing very rapid population growth and accelerating urbanization, without the requisite economy to produce the public and private resources necessary for housing, infrastructure and urban employment at the scales required.”

Unfortunately, alongside the runaway growth rate of urban centres, particularly in the developing world, there has been the equally disturbing increase in the number of people who do not earn enough to enjoy what is considered an acceptable level of living. It is this and other related attributes, that have recently shaped the form of the living environment – particularly in Sub-Saharan Africa – along the lines widely referred to as the “urbanization” and the “feminization” of poverty.

Today, estimates indicate that some 750 million urban dwellers worldwide, most of them in cities of the developing world, already live in “life-threatening conditions of deprivation and environmental degradation.”

Several studies, using economic indicators or human development indices, reveal that depending on the countries and towns, between 15 to 65 percent of African city dwellers, or about 40 percent of the continent’s 730 million people currently live beneath the poverty line. These people have very little or absolutely no access to the set of social and urban services that constitute decent living conditions. This has fuelled the belief that urban poverty in Africa is actually growing faster than rural poverty and is today one of the continent’s biggest challenges, with up to two-thirds of its urban population living in informal settlements without adequate sanitation, water, transport or health services.

However, other factors, such as the unintended consequences of trade liberalization, the collapse of productive industries in the face of unfair competition with cheaper imports and the downsizing of ancillary industries, are also known to have further stimulated the spread of yet another process tagged “informalization of the urban economy” (Urban Poverty Group Commission, 2004). This, in practical terms, refers to that situation whereby increasing shares of incomes are earned in non-formally regulated employment, in a process that actually results from the convergence of several economic processes.

The scenario of urbanization without economic growth has been blamed for the alarming level of growing unemployment and social exclusion that have made the informal sector the only escape route from chronic urban poverty for many in the developing world. In these areas, population growth, landlessness and fragmentation of land in the rural areas have also pushed many to turn to the urban centres to seek employment, thereby further
swelling the ranks of the urban poor, as the cities fail to meet the needs of these horde of job seekers.

While many of these migrants do not possess the required training or skills to key into the organized urban economy, even those that are trained usually find formal sector employment to be too highly competitive to offer solace to them. Thus, urban centres in much of the developing world, particularly Sub-Saharan Africa, are now daily besieged by a growing number of ill-equipped people who have no other option but to turn to the informal sector for their livelihoods, and they eventually simply end up as petty traders, hawkers or artisans, among others.

In most cities of the developing world, this growing mass of internal migrants, bitter, frustrated and eager to hit back at what appears to them an unfair world, also readily constitute a willing pool of fuel to mischief-makers seeking to precipitate instability, thereby constituting a contemporary security threat.

2. Nigeria: The Urban Economy

Nigeria, the most populous country in Africa with a land area of close to one million square kilometres, has a population currently estimated at between 126 to 132 million. Estimates at the turn of the 21st century suggest that 43.5 percent of the population already live in urban areas – up from 39 percent in 1985 – with projections that the urban population will reach 50 percent in just five years from now, by 2010, and 65 percent by 2020.

Some projections also suggest that the size and employment structure in the informal sector accounts for about 57.9 percent of the urban labour force, or more than double the 25 percent figure recorded in the mid-1960s. Life expectancy at birth is about 52 years; infant mortality rate is as high as 19.1 per 1,000; and the per capita income is thought to be in the region of US $274.00.

Geoffrey Nwaka (2005) writes that opinions differ widely on what should be the appropriate attitudes and policies towards the informal sector. Some of the more optimistic advocates of the sector tend to present it in romantic terms as a form of popular development, a vital source of employment and income for the poor, the seedbed of local entrepreneurship, and a potent instrument in the campaign to combat poverty and social exclusion. Critics, on the other hand, dismiss the sector as an anomaly, a source of disorder, and an obstacle to the development of a modern economy. They condemn the slums, health risks, insecurity and exploitation usually associated with the sector, and hope that like other transitory phases in the course of development, the informal sector will eventually wither away with time and economic progress.

Such views "dismiss earlier characterizations of the sector as easy to enter and requiring little money and skills, which led to the misconception that the informal sector required no form of official support. The views also condemn the large number of regulations and bureaucratic procedures from the different institutions and levels of government which tend to stifle entrepreneurship and to inhibit the realization of the full potential of the informal sector" (Nwaka, 2005).

Some who idealize the sector, however, also recognize that it could be at best a mixed blessing. They admit that "In-so-far as informal sector activities do not respect legal, social, health and quality standards, and furthermore do not pay taxes, they violate the rules of fair competition" (Nwaka, 2005). Indeed, they add, the informal sector has run its course, is now saturated, and may just be replicating the disguised unemployment that prevails in rural areas.

What cannot be in doubt, however, is that the informal sector remains at best a transitory vehicle and short-term buffer, which if otherwise rated, would constitute a misleading veneer that stunts long-term development and merely "postpones the evil day."

3. Nigeria: The Informal Sector

Nigeria's informal sector – almost comprising exclusively of small- and medium-sized enterprises (SME) but excluding those that are registered and tax-paying – accounts for about one-third of the country's GDP and as much as 90 percent of new job creation. With up to half the working population unemployed, the informal sector is often the only option for individuals seeking an income, or for that matter, to supplement their ordinarily inadequate income (see also section on Lagos informal sector voices and profile below). Thus, with anything from half to two-thirds of the population living on or below the poverty line, the informal sector can be said to be much more than a crucial lifeline.
Like in many other developing countries, the small and medium enterprise (SME) sector in Nigeria is considered crucial to job creation and broad-based economic development. In late 2004, an International Finance Corporation (IFC) study published by the Global Financial intelligence e-Magazine, The Banker (2004), narrowed down the barriers to small and medium enterprise (SME) development to three chief concerns. These are (i) inadequate physical infrastructure, particularly erratic power supply; (ii) an uncertain business environment – unsteady import and fiscal policies, corruption and red tape for instance; and (iii) insufficient access to finance. In addition, the IFC report mentions the fundamental role of information in the development of any viable entrepreneurship scheme. Since the onset of Nigeria’s civilian administration in 1999, the government’s reform programme has specifically focused on addressing the three barriers, although the lack of finance is considered a more complex problem.

The study, in summary, notes that Nigeria’s approach to SME financing in the past has varied and the results mixed. A major aspect of past attempts to tackle these problems was the establishment of specialized development finance institutions (DFIs) over the past two decades to provide capital to small businesses. These included among others, the Family Support Programme and the Family Economic Advancement Programme, both providing micro-credit to women; the National Directorate of Employment; the Peoples Bank of Nigeria (PBN) and community banks. Others are the National Economic Reconstruction Fund (NERFUND), the Nigerian Export-Import Bank, the Nigerian Agricultural Co-operative and Rural Development Bank, and the Bank of Industry.

The publication, The Banker (2004), notes that the establishment of the DFIs was essentially to address perceived limitations in the traditional financing mechanisms. Commercial banks were unable and reluctant to provide long-term credit to SMEs, in view of the short-term deposit base of these banks. By the late 1970s, commercial banks were actually compelled by the government to extend their services into rural parts of the country. However, “this was to prove unsustainable “as low incomes resulted in limited financial intermediation, both in terms of deposit-taking and lending. The banks’ commitment soon wavered and the business proved unprofitable”. There was also, at one time, a deliberate effort by the government, in the mood of the period, to fund the DFIs through government funds, following a global tendency whereby governments, as a deliberate policy, established schemes that provide concessionary financing to SMEs in recognition of their disadvantaged position in open market competition for finance and other resources.

4. Performance Assessment of Nigeria’s Approach to SME Financing

The following are the assessments of some key industry operatives on the government’s effort to improve access to finance for SMEs in Nigeria.

- Lawrence Osi-Afiana, Managing Director, Bank of Industry:

  “Despite the good intentions of the programmes, the institutions managing them later became weakened and incapable of effectively discharging their responsibilities.”

Constraints

- Weak capitalisation
- Inefficient operations
- Poor loan portfolio quality
- Poor liquidity and inability to access further external lines of credit
- Absence of accountability, and crippling bureaucratic practices

“The failure of the DFIs is traceable back to the fact that they operated with little commercial orientation. They operated on the philosophy that they were agents for the disbursement of government funds. Consequently, the beneficiaries of their facilities were not keen to service their loans even if they were able to, assuming the funds to be their share of the ‘national cake’.

Remedies

- For government-owned DFIs to be successful in the long term, they must (i) operate under a different philosophy that is underpinned by commercial orientation; and (ii) urgently embrace new approaches to financing SMEs, as past approaches have failed.
Modupe Adelaja, Director General, Small and Medium Enterprises Development Agency of Nigeria (SMEDAN):

"Access to finance has been difficult for SMEs but the availability of funds is only part of the equation."

Constraints
- DFIs in the past focused only on providing capital
- Did not give attention to assessing and developing SME managers, monitoring operational performance of the SME and mentoring inexperienced SME managers
- Financial institutions in Nigeria do not have the know-how and experience of dealing with SMEs

Prospects
- The Small and Medium Industries Equity Investments Scheme (SMIEIS), a private sector initiative of the Bankers Committee, consisting of the Central Bank of Nigeria and commercial banks, was launched in 2001
- Initially required all commercial and merchant banks to commit 10 percent of their annual pre-tax profit to the funding of equity investments in SMEs
- Stakeholders have since acknowledged that SMEs are often not suitable for equity investment as they lack the necessary structure
- Subsequently agreed that 10 percent of the 10 percent already set aside (or one percent of annual pre-tax profit) would be allocated to micro-credit
- By the end of April 2004, N22.3 billion (or about $167.7 million) had been set aside by 83 banks, of which N9.8 billion had been disbursed to 185 projects.

Senator Ibi Kunle Amosun, Member, Senate Committee on Commerce:

"Lack of technical capacity is a critical factor. Today, some 5,120 SMEs lack access to bank loans because of their inability properly to package themselves for loans."

- Current size of the Fund is about N35 billion that is accessible under the Small and Medium Enterprises Equity Investment Scheme.

Delta State Governor James Onanefea Ibori:

"The crisis of development in Nigeria is compounded not by lack of vision, but by consistent failure to actualise the goals for which different policies are made and agencies established. It is worsome that, in spite of the enormous resources and manpower available in the country, most economic policies fail to meet their goals."

Philip Oni, Chairman, National Bank of Nigeria:

"Since 1999, the promotion of SMEs has been accorded a priority status in government policy. This policy will sustain industrialisation and promote non-oil exports. Furthermore, it will achieve other economic goals of poverty eradication and employment creation."

5. The Lagos Economy: A Summary

Lagos State, one of the 36 constituent states of the Federal Republic of Nigeria, emerged first as a British colony in 1861 and attained statehood on May 27, 1967, when Nigeria's federation was restructured into 12 states.

Up until 11th December, 1991, Lagos served as both the country's Federal Capital and the seat of the state administration, over which time it transformed from a small fishing settlement to a burgeoning urban centre, boasting of a dense population and complex infrastructure. A highly urbanized state with more than 75 percent of its currently estimated 15 million inhabitants living in the metropolitan area, the state is labelled the largest conurbation in Africa, and with its population of 13.4 million residents by 1999, already considered the sixth largest mega-city in the world.

Population growth in Lagos, put at eight percent, is much higher than the national estimate of 2.9 percent and the global rate of two percent. Accounting for closer to one-third (27.4 percent) of the nation's total urban population, the city is said to be growing faster than both New York and Los Angeles in the United States.

Hence, managing the city with a population density of about 4,193 persons per square meter has transformed what would otherwise have been major socio-economic opportunities into critical challenges of urban governance for the managers of this unique city.
Some of the major economic attributes of Lagos state are that even after losing the seat of federal power to Abuja, it remains the commercial nerve centre for the nation and the entire sub-region, and hosts over 65 percent of Nigeria's industries. The state also boasts of over 10,000 commercial concerns; over 250 financial institutions; and up to 22 industrial estates and several business districts. It also accounts for nearly 60 percent of the country's Gross Domestic Product (GDP) and over 65 percent of national investment. Urban poverty levels of between 51-55 percent (male) and 55-62 percent (female) have been recorded across the state, compared with national poverty estimates of about 70 percent.

6. The Lagos Informal Sector Voices and Profiles

<table>
<thead>
<tr>
<th>Ismaila Aderounmu</th>
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<td>(carpenter, 39 yrs old, married)</td>
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**Qualifications:**
Trained for 4 years as apprentice; been on his own since 1987 (18 years)

**Income:**
N 3,000–N 4,000 ($22–$30) total turnover/day

**Social Obligations:**
Doesn't pay tax, but pays for trade permit and rents shop space (responds to survival needs)

**Handicaps:**
Under constant threat of eviction from landlord; constantly rising production costs; unsteady power supply

**Priority Needs:**
Access to land; secure tenure; stability in business environment; regulated local charges

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<th>Bashorun Alimot</th>
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<td>(dress-maker, early 30s, married)</td>
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**Qualifications:**
Attended government-approved training school at personal expense; has been in the trade for 6 years

**Income:**
Average N 2,000 ($15) total turnover per day

**Social Obligations:**
Doesn't pay tax, but pays for trade permit and rents shop space (responds to survival needs)

**Handicaps:**
Unsteady power supply; unsteady patronage

**Priority Needs:**
More money in circulation to boost patronage
7. Challenges to Informal Sector Development

Cities of the 21st century have been described as engines of development which incubate innovations, ideas and change for transmission to the hinterland. To perform this role, the importance of efficient urban planning support with functional infrastructure, such as appropriate provision of layouts for not only heavy but also light industries, efficient transportation and other basic services cannot be overemphasised. From the foregoing therefore, it is clear that despite the potential offered by the informal sector to act as a catalyst for stimulating economic growth and rejuvenation of the city, several challenges exist which limits its ability to achieve this function.

Some of the most common limitations, as highlighted above, are:

- Weak and sometimes non-existent regulatory mechanisms, which neither curbs their penchant for subsistence operations nor provide guidance to enable them to upgrade into the more integrated sectors of the economy;
- Low productivity and incomes, on account of the inability to utilise the value of the limited capital owned;
- Size of sector also indicates a failure of general socio-economic policies;
- Level of investment is generally very low, thereby limiting capacity to cater for the demand for high job creation stimulated by the large number of unskilled rural migrants;
- Large attraction to females due to gender bias in employment opportunities in the formal sector, among others.

8. Incentives for Informal Sector Development

Some of the major incentives for the development of the informal sector include:

- Access to funding, land, security of tenure;
- Stable power supply and provision of basic services;
- Consistent growth in formal sector to ease pressure on informal sector activities;
- Adoption of innovative, easy-access funding mechanisms to boost investment in the sector at household level;
- Public re-orientation with regard to improving understanding on the essence of taxation;
- Deliberate effort by government to ensure collection of taxes, through door-to-door mop-up and strict enforcement to prompt survival instincts among operatives;

Enhancing Resource Allocation to Urban Development in Africa
Harmonization of local authority charges;
- Economic stability and consistency in government policy;
- Restructuring of government-owned DFIs to operate under a different, sustainable philosophy.

9. Conclusion

The characteristics, limitations and prospects of the operations of the informal sector have been discussed through the prism of the Lagos experience. The limitations are substantial, but so are the prospects, if adequately harnessed.

Nigeria’s informal sector, which if appropriately addressed could form the catalyst or fulcrum for economic development, has failed to provide upward mobility to its members in its present form, and has limited their ability to transit into formal sector operations in the future.

It has been rare, in the Nigerian context at least, to find sufficient instances of informal activities transforming into small-scale enterprises and eventually integrating fully into the formal cadres of the economy. Indeed, many have grown to be rather profitable activities, but many consider it the exception rather than the norm, to find these activities rising to become a chain of companies, for instance, or even becoming noteworthy references of truly motivating templates for business development. There does not appear to be many small enterprises that have been able to undertake this transformation, as it seems to have happened in Kenya.

Any city or state which does not have the goal of providing greater opportunities to the informal sector as a primary objective, despite whatever other promising incentives exist, is likely only to remain grounded in the mire of underdevelopment.

References


PART III. ANNEXES

Aide-Memoire

1. Background and Justification

Cities are engines of economic growth and social development, drawing in human resources, raw materials and capital which, combined with more sophisticated urban infrastructure, have been the driving force behind national economic development in most countries. Furthermore, as stressed in a previous State of the World's Cities report published at the beginning of the new millennium, the "urban economy is the hub and nerve centre of the national economy and, as the global society expands, a nation's welfare will be determined increasingly by the roles its cities play in the global economy." 

This prediction is not surprising considering that the world's economic history during the last century showed that the processes of urbanization and economic progress tend to be mutually reinforcing. The experiences of most developing countries during the 20th century showed in particular that urbanization was closely associated with increasing levels economic growth, income and social progress. For example, a comprehensive study of 90 countries from 1960 to 1980 provides evidence that the urban share of the population increases with national income per capita.

Aggregate data are clearly supported by numerous country studies in all developing country regions concluding that "cities, especially bigger cities, mean higher productivity and higher per capita incomes." Once again, this is not surprising, given that cities provide the economics of scale and agglomeration, as well as the socio-economic infrastructure, necessary for the acceleration of national economic growth.

At the same time, cities are also engines of rural development, since urban markets provide powerful incentives for increased rural production and, conversely, expanding rural markets provide some incentives for the increased output of goods and services produced in urban areas. Suffice it to say that most countries face a significant degree of economic and social interdependence between urban and rural areas, and thus require a more balanced and mutually supportive approach to their development.

In a nutshell, urban-rural linkages involve the growing flow of public and private capital, people (either migrants or commuters) and trade of goods and services between urban and rural areas. In addition, there are three critical economic flows between urban and rural areas: the flow of ideas, the flow of information and the diffusion of innovation. This evolving approach – which is often referred to as the "urban-rural linkage development perspective" – is increasingly recognized as a key national development policy, notably in developing countries with vibrant urban areas.

However, despite the widespread evidence that cities are engines of economic and social change, it is also surprising that "urban growth and the urban share of the national economy ... are rarely recognized in global debates about economic and development policy." There is now evidence to show, for example, that urban economic activities account for more than half of Gross National Income (GNI) in all countries, and up to four-fifths or more in more urbanized countries in Latin America, Asia and the developed world.

While the African continent is characterized by a broadly different picture, a certain degree of convergence with other regions is beginning to be experienced with regard to key cities in several countries in the eastern,
northern, southern and western Africa sub-regions, such as Addis Ababa, Cairo, Cape Town, Casablanca, Dakar, Johannesburg, Lagos and Nairobi. For example, while Nairobi is inhabited by approximately 5.2 percent of Kenya’s population, its share of GNI is almost four times greater. Similarly, a recent publication on the role of cities as engines of economic development stressed that while African cities contribute to 60 percent of the continent’s Gross Domestic Product (GDP), they account for only 34 percent of its population.

There is, therefore, an urgent need to enhance the role of African cities as engines of economic growth and development, including through a better-targeted allocation of national budgetary resources to the development and management of cities and towns.

2. Objectives

The immediate objective of the regional seminar is to promote awareness among and thus sensitize African decision- and policy-makers – notably in the planning, budget or finance ministries and departments – of the need to enhance resource allocation to key African cities as a means of accelerating national economic growth and development, generating greater employment and increasing incomes.

It envisages doing this by sharing experiences of selected cities that play key roles in national economic growth and development, against the background provided in the recently published UN-HABITAT report on “Cities – Engines of Economic Development.” The participants are expected to share their countries’ and cities’ experiences, review current practices in this area, compare notes across cities and countries and to make recommendations on how resource allocation could be enhanced towards more effective and productive urban development.

3. Thematic Structure and Organizational Approach

Following opening addresses by senior UN-HABITAT members and a representative of the host country government, the seminar will be divided into consecutive thematic sessions (during the first day) and country or city presentations, in the second day.

A broad presentation on the role of African cities as engines of economic development will be followed by thematic sessions on (a) municipal finance and the provision of urban infrastructure; (b) municipal regulation and the role of the informal sector; and (c) the role of the formal private sector in ongoing processes of economic globalization.

Although it is recognized that more work needs to be undertaken at the national level on the role of cities as engines of economic development, participants will be expected to provide experiences of their respective national efforts to enhance that role, the problems encountered and the lessons learned in their respective countries, as well as further measures required to strengthen that role. Provision shall therefore be made for presentation of individual country and city experiences by selected participants.

In addition, representatives of the print and electronic media are expected to reflect their perspective on the issues under discussion and to contribute to disseminating the outcome and recommendations of the seminar.

For its part, UN-HABITAT will elaborate the issues developed in the above-mentioned report, as well as update and synthesize national experiences. These national experiences shall constitute the background papers of the seminar.

4. Expected Outcome

The outcome of the seminar is envisaged to include:
(i) Improved awareness of the economic developmental importance of cities and the need for enhancing resource allocation to strengthen the potential role that can be played by African cities in accelerating national economic growth and social development, including through greater employment and income generation.
(ii) Sharing regional experiences and lessons with a view to stimulating mutual learning and capacity-building, as well as sensitizing greater numbers of decision- and policy-makers – at both national and local levels – to the importance of allocating greater resources to strengthen the role of cities as engines of economic development.

(iii) Identification of policies, strategies and approaches to bring about enhanced budgetary and human resource allocation to increase the positive impacts of urban growth as a lever of national economic development.

5. Participants

The seminar is expected to be attended by national government policy/decision-makers, notably those belonging to finance, budget and planning ministries; urban development planners and municipal managers or administrators; researchers and practitioners dealing with urban development and municipal finance; members of the media specializing on urban development and municipal finance; as well as representatives of international organizations, bilateral agencies and civil society.

There will be participants from countries representing the four major geographical sub-regions of the continent, namely eastern, northern, southern and western Africa.

Intending participants who wish to prepare and present papers on any aspects of the theme should ensure that the paper reaches the organizers listed below by 10 October 2005.

6. Venue, Date and Official Language

The regional seminar is being organized by UN-HABITAT. The date and venue of the seminar are as follows:

(i) Date: 2-3 November 2005

(ii) Venue: Conference Room 8, United Nations, Gigiri, Nairobi, Kenya

Given limited budgetary resources, the language of the seminar shall be English.

7. Registration

All participants are requested to register on the first day of the seminar. All relevant documentation will be available at the registration desk.

8. Communication

All inquiries concerning the seminar should be addressed to the seminar convenor:

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9. Provisional Programme of Work

Wednesday, 2 November
08:30 – 09:30  Registration
09:30 – 09:45  Introductory remarks by Dr Don Okpala, Director of Monitoring and Research Division, UN-HABITAT
09:45 – 10:00  Welcoming remarks by the Executive Director of UN-HABITAT
10:00 – 10:15  Welcoming remarks by His Worship Dick Wathika, Mayor of Nairobi
10:15 – 10:30  Key address by Hon. Musikari Kombo, Minister for Local Government
10:45 – 11:00  Coffee Break
11:00 – 11:30  Thematic Presentation I: “Enhancing the role of cities as engines of economic development.” by Dr Ananda Welwitsa, UN-HABITAT
11:30 – 12:30  Discussion moderated by Prof. A.C. Mosha, University of Botswana
12:30 – 14:00  Lunch
14:00 – 14:30  Thematic Presentation II: “Mobilizing public finance for city development and management in African countries.” by Prof. A.C. Mosha, University of Botswana
14:30 – 15:30  Discussion moderated by Mr Hannock Kumwenda, Ministry of Economic Planning and Development, Malawi
15:30 – 16:00  Coffee Break
16:00 – 16:30  Thematic Presentation III: “Mobilizing private investments and other domestic resources for urban development in Africa”, by Mr Wafula Nabutola, Chairman, Nairobi Central Business District Association
16:30 – 17:30  Discussion moderated by Dr Sterga Tax-Bamwenda, Office of the President, Tanzania
18:00 – 20:00  Reception hosted by UN-HABITAT

Thursday, 3 November
09:30 – 10:00  Thematic Presentation IV: “Incentives and support to the development of the informal sector in African cities,” by Mr Paul Okunlola Onyeniran, Assistant Editor, The Guardian, Nigeria
10:00 – 10:45  Discussion moderated by Ms Jacquie Subban, eThekwini/Durban Municipality, South Africa.
10:45 – 11:00  Coffee Break
11:00 – 11:30  Western Africa – National and City Presentation(s)
11:30 – 12:00  “The case for a balanced urban-rural mix in resource allocation- a look at the city situation in Nigeria” Mrs Chinedu Brown, Abia State Budget and Planning, Nigeria. Discussion [moderated by UN-HABITAT]
12:00 – 12:30  Southern Africa – National and City Presentation(s)
- “Economic development strategy: City of Durban”, Ms Jacquie Subban, eThekwini/Durban Municipality, South Africa. Discussion [moderated by UN-HABITAT]
12:30 – 13:00  Lunch
13:00 – 14:00  Coffee Break
14:00 – 14:30  North Africa – National and City Presentation(s)
- “Local economic development in Alexandria”, Dr. Ayman El-Hefnawi, Urban Training and Research Institute, Cairo.

Enhancing Resource Allocation to Urban Development in Africa
14:30 – 15:00  Discussion [moderated by UN-HABITAT]
15:00 – 15:15  Coffee Break
15:15 – 15:45  Eastern Africa – National and City Presentation(s)
   - “Financing of urban local governments in Uganda”, Mr. Tom Nkayarwa, Ministry of Local Government, Uganda
   - Allocation of financial resources to Urban Authorities in Tanzania, Mrs. Tarashi Kibenga, Office of the President, Regional Administration and Local Government, Tanzania.
   - “Profile of Addis Ababa and development endeavours of the city”, Mr Zemedkun Girma, Addis Ababa City Council
15:45 – 16:15  Discussion [moderated by UN-HABITAT]
16:15 – 16:30  Summary and Recommendations of Seminar
16:30  Closure of Seminar
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