

The financing of city services in Southern Africa

This case study draws on research that investigated the financial sustainability of cities in the Southern African region (SACN, 2011). The research was undertaken by the South African Cities Network (SACN). The project was jointly sponsored by the Public Private Infrastructure Advisory Facility (PPIAF) and the World Bank Institute (WBI). See Sheet 5 for reference details. The contribution by SACN of the material for this document is gratefully acknowledged.

An introduction to the case study is given below. See page 2 for reflection and learning activities. You can do these activities on your own or in groups, as appropriate for your learning session. Look at the activities before you begin so you know what to look out for during your reading.

Sheets 2-4 of this case study present an outline of the many challenges of financial sustainability and effective service delivery facing Southern African cities. It comments on issues such as rapidly growing populations of mostly poor people who do not form part of local revenues, of limited city authority and human resource capacity. Importantly it points to limited effort made by many cities to bring in more revenue and highlights this as a significant opportunity for improving city finances. A summary of the key findings of the study and some of the recommendations arising from it are given on Sheet 5.

Learning outcomes

By the end of this session participants will be able to:

- Describe key challenges facing Southern African cities
- Identify core issues obstructing progress towards financial sustainability of Southern African cities and effective service delivery
- Make proposals for concrete and achievable steps towards achieving such improvements.

Background to this case study

In 2010 the SACN, in conjunction with the WBI and the PPIAF, implemented a project to support the emergence of a sustainable municipal finance market in Southern Africa.

The aim of the project was to promote more effective city financial planning and management, better credit ratings and improved access to capital markets for infrastructure investment purposes. The project involved conducting a series of 'shadow' credit assessments of city governments in Southern Africa and developing a customised financial management capacity building programme for senior city management teams.

Information was gathered by means of interviews, questionnaires, documentation and financial data during a series of visits to city governments across Southern Africa. A total of 14 city municipalities in nine countries were visited. The cities were chosen using considerations of city size, geographical spread, potential creditworthiness, and project logistics and budget. Ten cities are included in the report: Dar es Salaam, Port Louis (Mauritius), Lusaka, Windhoek, Gaborone, Maputo, Arusha, Lilongwe, Blantyre and Ndola. The trends observed in these Southern African cities are applicable to many other cities across the continent and much of what is presented here can be generalised.

Southern African countries each have their own constitutional framework and system of intergovernmental fiscal relations. The formal and legal position of city governments, and their expenditure responsibilities and revenue-raising powers, reflect the economic, social and political histories of the countries concerned. Thus, for example, Maputo operates within a Lusophone legal framework and tradition, which is very different from the Anglophone equivalent that applies in Blantyre.

But many commonalities exist and it is these that inform the core arguments and recommendations.

Part of a series of case studies developed by Urban LandMark as a teaching and learning resource for studies in urban land markets. Urban LandMark gratefully acknowledges funding by UKaid from the Department for International Development (DFID). Email: info@urbanlandmark.org.za • www.urbanlandmark.org.za

Learning activities

Before you start

Before you read the case study, spend a couple of minutes making a note of your answers to this question:

In your opinion or experience, why do Southern African city governments seem unable to address the infrastructure development and service delivery demands that are their duty to address?

After reading the case study

Do the following activities on your own, or in groups. Write down your answers to the questions. Be prepared to share your findings with the larger group.

1. What are the main challenges facing developing country cities (and in Southern Africa in particular) regarding funding of operations, and infrastructure maintenance and development?
2. The work that this case study is based on focussed on 'shadow' credit assessments. If you were a consultant appointed to support a follow-up implementation phase that is intended to improve creditworthiness and strengthen city budgets:
 - a) What key elements would you choose to prioritise?
 - b) What operating, budgeting and management guidelines would you propose?
3. What tangible and achievable proposals would you make for achieving effective infrastructure development and service delivery?

Reflection

- Do you have any core beliefs that were challenged in this case study? What were they? Share this with the other participants using this learning material.
- What are the key insights that you have gained from this case study?

The challenge

The obligation to deliver infrastructure and services is an ongoing challenge for Southern African cities. According to the report *Africa's Infrastructure: A Time for Transformation*, to meet Africa's infrastructure needs will require an annual investment of US\$93 billion, of which two-thirds will be spent on capital expenditure and the balance on operations and maintenance. Much of this expenditure needs to happen in cities, as cities are (and will increasingly be) the drivers of social and economic development.

This case study opens with a series of 'city snapshots' that provide insights into the nature of this challenge. It then explores some of the major constraints that prevent cities from being fully sustainable and from providing comprehensive and effective services.

City snapshots: an overview of the challenges

These snapshots cover some of the challenges facing Southern African cities under key themes:

- rapidly growing populations put huge pressure on service delivery
- low income levels imply a low revenue base
- service delivery challenges
- large city populations with smaller economies are not sustainable.

Photo: SACN



Municipal offices in Port Louis

Rapidly growing populations

Most Southern African cities have rapidly growing populations. This creates huge challenges for city governments, especially in the area of service delivery.

In 1965, at independence, **Gaborone** became the capital of Botswana. The population, which was under 4 000 people in 1964, rose to 224 000 by 2001. Gaborone now doubles in size roughly every 10 years.

Lilongwe has a population of approximately 700 000 people and an additional daily commuter population of about 300 000. Around 70% of the city population live in unplanned areas. Lilongwe's high population growth rate is due mainly to in-migration, which poses a substantial challenge for city financing of future services as the average income of the migrants is relatively low.

Photo: SACN



Rapidly growing populations

The Municipal Council of **Port Louis** serves an area of 45.5 square kilometres, which is inhabited by 150 000 people. However, the concentration of economic activity in the city means that the daytime commuter population can amount to an additional 300 000 people. This number is growing faster than the residential population. This has significant implications for planning, revenues and road congestion.

In 2000 **Lusaka** had a population of 1.08 million, which had risen to 1.46 million by 2010 and is currently estimated at over 2 million people. Its current population growth rate – around 3.2% per year – is one of the highest in the region.

Maputo is a city of about 1.4 million people. However, if the many informal settlements on the outskirts of the city are included, the total population is estimated to be significantly higher, of which almost 70% live below the poverty line.

Dar es Salaam is home to one-tenth of the national population, with a current population of above three million (almost eight times larger than Arusha, the next largest city). It is one of Africa's fastest-growing cities with a population growth rate of nearly 5% per year.

In conclusion, rapidly growing city populations, whether from internal growth, in-migration or daily commuting, present major challenges to the provision of services. The difficulties here are the pace at which populations are growing and the fact that most people, particularly newcomers to cities, are in informal settlements, which are difficult to service.

If the many informal settlements on the outskirts of Maputo are included, the city's total population is estimated to be significantly higher than 1.4 million people, of which almost 70% live below the poverty line.

Low income levels imply a low revenue base

Most of the people living in Southern African cities are poor. This means there is a low revenue base for cities to draw on. The rapidly growing populations mentioned above exacerbate the problem. However, it should be noted that many Southern African city economies are currently growing and businesses likewise. This represents a strategic opportunity to address the above challenge.

About 68% of **Zambians** live below the poverty line, with rural poverty rates at 78% and urbanised rates at 53%. According to the United Nations Human Development Index, Zambia is the ninth poorest country in the world.

Photo: SACN



Small-scale commercial activities thrive but are mostly below a taxable threshold

About 65% of the local economy of **Lusaka** is in the informal sector. Nearly one-quarter of Lusaka's inhabitants were not born in the city, 70% of the city population are below the age of 30, and 57% are below the age of 20. The rapid growth of the city is associated with more informal settlements and a general degradation of the quality of the urban environment. Slum dwellers make up an estimated 50% to 60% of the urban population of Lusaka.

A serious challenge for the **Windhoek** City Council is an unplanned settlement of approximately 40 000 people near Katutura to which services must be extended. But the people living here are poor and unable to pay for services. Extending services, at the standards requested by national government, is likely to threaten seriously the financial sustainability of Windhoek, if no support is forthcoming from national government.

What these examples highlight is that most people in these cities are very poor. They fall below the threshold for local taxation, yet they need services. This places a severe drain on city revenues.

Service delivery challenges

Most of the cities in Southern Africa have huge service delivery backlogs, making it very difficult for city governments to catch up with need and demand.

Dar es Salaam faces substantial service delivery challenges: more than 70% of the city's population lives in unserviced and unplanned settlements; more than 60% of solid waste is not collected; massive traffic bottlenecks are caused by the absence of secondary roads; and a lack of surface water drains leads to regular flooding, with associated public health risks.

Rapid population growth in **Arusha** is increasing pressure on (and demand for) services, while offering limited ability to raise revenues to pay for the expanded services.

Lusaka has a significant infrastructure backlog: in 2003, 74% of residences had no access to piped water, 82% had no access to sanitation and 56% had no electricity supply. In 2005, 56% of the estimated 200 000 households used charcoal, kerosene and wood as fuel. The lack of infrastructure is attributed to a lack of investment into the city during the years of economic decline in the 1970s and 1980s. Lusaka consumes about 220 000 cubic metres of water a day and is estimated to have a daily water deficit of 80 000 cubic metres. Access to water and sanitation has deteriorated.

Most of the cities in Southern Africa have huge service delivery backlogs, making it very difficult for city governments to catch up with need and demand.

Large populations with relatively small city economies

Photo: Urban LandMark



Kibera, outside Nairobi

Another challenge facing Southern African city governments in relation to revenue issues is the nature of most of the region's cities.

The world's cities can be placed into size categories: The first four are 'megacities', or metropolitan areas (over 10 million people), 'large middleweight' cities (5 million to 10 million),

'midsize middleweight' cities (2 million to 5 million), which includes Johannesburg, Dar es Salaam and Cape Town and 'small middleweight' cities (150 000 to 2 million), which includes the remaining cities listed in the case study.

These distinctions are significant because they relate both to the spending-side challenges (higher populations and larger economies require more and higher-order services) and to the potential local tax resources available to meet those challenges. Where the population size does not yield higher incomes and is not matched by higher or more extensive provision of services, especially higher order services, one then finds more intense infrastructure and service delivery breakdowns, and greater attention is required. Knowing this in advance is a major advantage for city management.

What we learn from this analysis is that although cities like Port Louis, Gaborone and Windhoek have small populations with relatively large local economies, and others like Dar es Salaam and Lusaka have large populations with proportionately large local economies, there is a middle group of cities, namely Arusha, Ndola, Lilongwe, Blantyre and Maputo (and others like them across Africa) that have populations that are disproportionately large compared to their economies. It is these cities that face the biggest challenges of financial sustainability and in terms of their ability to provide services.

Many Southern African cities have populations that are disproportionately large compared to their economies. It is these cities that face the biggest challenges of financial sustainability and in terms of their ability to provide services.

Constraints on effective city management

Notwithstanding the 'city snapshots' provided earlier, one needs to examine in more detail the significant constraints militating against effective city management.

This section discusses some of the cross-cutting financial issues and themes affecting Southern African city governments. Although the diversity of the cities prevents too ambitious a discussion, some generalisations are recognisably true of many, if not most, of the city governments. The perspective adopted is that cities make possible the clustering of complementary economic activities, intellectual and financial capital, and cultural and entrepreneurial energy, thus raising overall productivity and under-pinning long-term social and economic development. A successful and well-functioning city needs effective infrastructure and built environment services over the entire spectrum; in turn, this requires sound organisational and governance arrangements and adequate resourcing.

What follows is an outline of city finance themes that are arguably of concern to many or most of the city governments under discussion. The themes covered here are:

- limited city powers and functions, especially in relation to the built environment
- limited city human resource capacity
- limited city decision-making and autonomy
- limited city revenue effort.

A successful and well-functioning city needs effective infrastructure and built environment services over the entire spectrum; in turn, this requires sound organisational and governance arrangements and adequate resourcing.

Limited city government powers and functions

A trend in most countries under review here, and beyond these, has been to systematically strip functions from city governments. Many national governments choose to allocate water and electricity distribution responsibilities to national utilities rather than to city governments. In Southern Africa, therefore, most city governments are not responsible for many of their own built environment functions.

For example, until 1972 local governments in **Zambia** generally had little difficulty in fulfilling their expenditure obligations, due to a strong capacity to generate their own revenue from many significant sources including electricity distribution, water supply, rentals and other sources. There followed a long period of local government decline, which was due to multiple factors including the removal of income-generating functions without compensation; the assignment of additional expenditure responsibilities without concomitant revenue resources; urbanisation, which has tended to increase local fiscal pressures, again disregarded by national government; and declining management capacity among municipalities.

Thus, in 1971 electricity distribution was removed from city councils. Then in 1996/97 water supply functions were moved into regional utilities, housing stock was sold off at below market value by central government decree and responsibility for general health services was removed from city councils. This had the effect of removing an important source of revenue for local authorities.

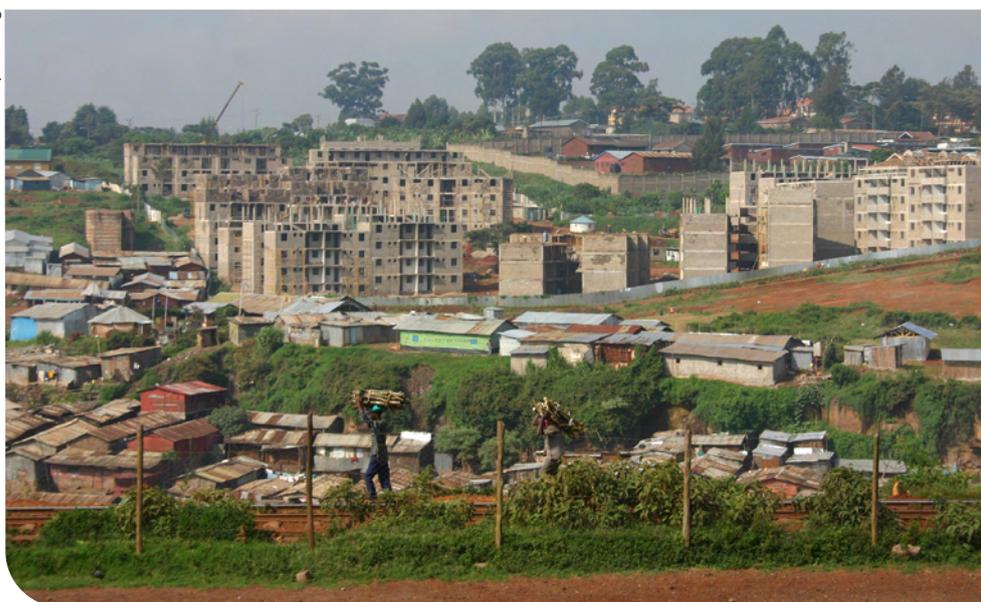
Photo: Urban LandMark



Electricity services usually benefit national utilities, not local city economies

Similarly in **Namibia**, current national policy is to remove electricity distribution from city responsibilities, the net impact of which is likely to be financially negative for Windhoek. This functional and financial 'emasculatation' of city governments can be ascribed to many causes. Government may argue that the most effective way to deliver those services is through national utilities, and there may be a lack of confidence in city councils. In some cases national governments may have systematically weakened city governments because of the potential for urban voters to elect opposition parties. Furthermore, the establishment of new utilities may provide opportunities for well-connected elements in the local business class. Alternatively, this 'emasculatation' may simply be due to a general lack of appreciation of the importance of effective city government.

Photo: en.wikipedia.org



City revenues cannot cope – housing built using external funding

Limited city human resource capacity

Almost all of the city governments participating in the project acknowledged significant human resource capacity constraints and skills deficits, particularly in specific, often technical, areas. Even in some of the more effectively run cities, a number of senior officials with long experience in technical services are approaching retirement and will not be easy to replace. Yet there was almost no sense of the necessity of a significant programme to address this gap. Instead city governments tend to 'live with' their skills and capacity shortages. The problems arise when senior administrative positions are filled on an 'acting' basis for extended periods. This phenomenon is almost universal.

Most Southern African cities discussed in this case study have very limited decision-making authority.

Limited city decision-making and autonomy

Most cities discussed in this case study have very limited decision-making authority. All must have their budgets approved by national government, and they all also have various external reporting requirements. City government borrowing almost always requires national government approval, and tax and tariff decisions frequently need central approval.

Central decision-making on city issues can also extend further, to staffing and tariff decisions. In **Malawi**, a Local Government Service Commission makes all city staff appointments, the national president appoints city Chief Executives, and tariff increases require national approval.

In **Tanzania**, senior officials are appointed by central government. Appointments for municipal posts take place through a central government Recruitment Secretariat. All municipal employees can be transferred at any time by central government.

The effect of managing human resources in this way is to make city governments extensions of central government, particularly when senior-level staff are re-assigned around the country and between government bodies. It reduces management understanding of, and commitment to, solving city issues, and may also weaken accountability and concern for the weak financial and service delivery position of the city government.

Centralised financial decision-making can have other effects on city government issues. For example, national restrictions on tax rates and tariffs weaken city revenue flows. Ideally city governments should manage their own relationship with their residents, including the setting of tariffs. Furthermore, national government involvement in city finances tends to weaken local accountability for any funds raised.

Limited city revenue effort

In general, city governments in Southern Africa do not come close to maximising the cash revenues available to them with their existing revenue powers. The billing itself is often very inefficient and collection rates are low. Property taxes play a critical role in the revenues of city governments (in particular those that cannot rely upon government grants) and yet in most instances they should be yielding considerably more revenue than they do at present.

For example, **Lilongwe** derives 70% of its income from property tax alone. The valuation roll currently lists about 35 000 properties, and city management indicates that perhaps another 45 000 properties should be on the valuation roll but are not. This suggests that substantial potential exists to increase property tax billings by two-thirds or more, by ensuring that the valuation roll is complete and accurate.

This example highlights a key element of the failure of cities to collect the revenues that are due to them. Property registers or valuation rolls are badly out of date in most cases, often up to 10 years or more. Ideally, revisions of the valuation roll should take place annually.

Arusha contains approximately 20 000 properties, but only 7 000 of these are taxed. Property tax invoices are hand delivered annually in December, and property owners are given three months to pay. The overall collection rate is estimated at around 30%. Put differently, only 35% of properties are taxed and only 30% of these taxes are collected. This computes to a revenue return of 10.5%. Efforts to improve this rate have focused on an annual Revenue Task Force which goes from house to house enforcing collections.

The fact that existing revenue sources, such as property taxes, should be yielding considerably more cash revenue than they do is one of the critical issues facing many city governments in Southern Africa. This reflects profound governance issues, including the weakness of the relationship between city government as service provider and the resident or business as service recipient and payer of taxes and service charges. It also offers optimistic possibilities for the future – the solutions are not actually all that complex and come down to putting fairly basic management procedures in place and seeing that these are followed through.

A positive ending?

The reader is reminded of the point made earlier that many African city economies have been growing, and likewise businesses. This represents a significant missed opportunity for revenue collection. The following table from Hunter (2012) showing annual economic growth in the 6-year period from 2006 to 2012 illustrates this point. These figures translate to per annum growth rates of 7% p.a. for Abuja to 11% p.a. for Luanda. These are huge growth rates. These new sources of revenue could be drawn on to improve the sustainability of these cities. Sadly, as the SACN research points out, not a lot is being done to address this situation.

City	% change (2006-2012)
Luanda	88.5
Kumasi	76.0
Accra	73.0
Addis Ababa	69.7
Yamoussoukro	67.0
Matola	66.2
Dar es Salaam	63.6
Bobo-Dioulasso	63.2
Lilongwe	62.6
Oagadougou	62.1
Blantyre	57.9
Kitwe	56.1
Nampula	53.6
Abuja	51.5

Photo: Kevin James / Urban LandMark



City economies in Southern Africa are growing

Summary sheet

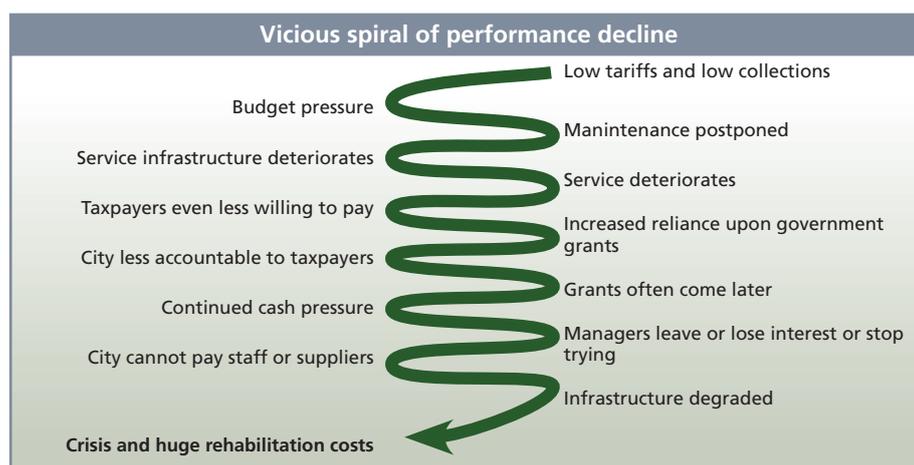
Summary and guiding principles for recommendations

City governments in Southern Africa vary in population and economic size, and in government expenditure and revenue assignments. Recent financial performance, and indeed potential creditworthiness, also vary greatly, ranging from cities where a weak economic base and poor governance arrangements would lead to poor ratings, to cities with stronger local economies and better administrative and governance arrangements that should be able to sustain better creditworthiness.

However, a number of themes appear to be characteristic of many or most of the city governments discussed, with some exceptions. The following can be said to characterise many of the city governments in Southern Africa:

- under-empowered with respect to built environment services
- under-resourced, yet inadequate revenue effort (underperforming revenue administration)
- under-capacitated with respect to key skills, yet no significant programme to address this
- over-controlled with respect to staff appointments, tariff increases, etc.

These two diagrams encapsulate the key lessons from this case study. The first starts at the top right side and spirals down. It describes what happens when the challenges described above are not addressed. The second diagram reverses this. These two summary diagrams are followed by a set of lessons and recommendations.



A critical but unstated element of this recovery spiral is having people within city management willing to make it happen. Without that, no amount of technical support will make any difference.

Lessons and recommendations

Some useful lessons and experiences of innovation in financial management have been learned from the cities that participated in the survey. While they are diverse, there are many commonalities. The worsening international economic conditions in recent times highlight a common vulnerability among these diverse cities. There is also a universal need for people to live in a financially well-managed city that provides services to all. To achieve this, many of the municipalities and their respective national governments need to tackle a number of common challenges. Municipalities need to have sufficient financial and decision-making autonomy to deal adequately with the growing urban demand for services. Greater effort also needs to be expended at revenue collection.

The SACN report (2011) makes the following comparatively simple propositions for improving the financing of city services in Southern Africa:

- Cities are already, and will increasingly be, the critical sites and drivers of social and economic development. Such development requires and depends on effective urban services for city inhabitants and businesses.
- Built environment functions are essential city government functions, necessary to support city residents and city economies, and city governments should have clear and substantial built environment mandates.
- City governments, more than other municipalities, should be able to finance much of their built environment services through appropriate local revenue resources and should accordingly be allocated sufficient local revenue authority, including taxes on property and local business activity, and services charges.
- City governments need to develop and maintain an implicit social contract with city households and businesses, in terms of which the full potential of assigned revenue sources is achieved (which means taxes and service charges are paid) and good quality services are delivered.
- City economies, as well as the number of better-resourced households and businesses in cities, have been growing. This growth represents a significant resource that can and should be exploited.
- City governments need an adequately funded capital investment plan, ideally from own revenue sources. Intergovernmental fiscal arrangements should provide strong incentives to maintain capital assets.
- Although often under-rated, good financial management and creditworthiness are worthy objectives for city governments and together can improve access to capital infrastructure funding.
- For city governments to be truly financially resilient, administration and service delivery, together with an effective city social contract, should create the correct environment and platform for social development and economic growth. In many cases, this will require a city leadership with the political stature and maturity to be able to drive through administrative, financial and revenue reforms.

Further reading

Hunter R (2012) *Municipal Finance in African Cities*. Presentation made at a Regional Capacity Building Forum of the African Centre for Cities/Cities Alliance 'State of the Cities in Africa Project', 20-22 September 2012, Cape Town, South Africa.

SACN (2011) *The Financing of City Services in Southern Africa*. SACN, Johannesburg.
<http://www.sacities.net/knowledge/research/presentations>