

**IMMEDIATE  
ATTENTION**

SM/13/61

March 12, 2013

To: Members of the Executive Board

From: The Secretary

Subject: **Global Monitoring Report 2013—Rural-Urban Dynamics and the Millennium Development Goals**

Attached for consideration by the Executive Directors is the 2013 Global Monitoring Report—rural-urban dynamics and the Millennium Development Goals, prepared jointly by the staffs of the Fund and the World Bank. It is not proposed to bring this report to the agenda of the Executive Board for discussion unless an Executive Director so requests by **noon on Tuesday, March 19, 2013**. The report is to be discussed by World Bank Executive Directors at a meeting of the World Bank's Committee of the Whole scheduled for March 21, 2013.

Following the discussion, the report will be revised as necessary and published. The overview will be distributed to the Development Committee as a background document.

Questions may be addressed to Ms. Pattillo (ext. 37319) in SPR.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

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Department Heads



# **Global Monitoring Report 2013**

## **Rural-Urban Dynamics and the Millennium Development Goals**

**March 2013**

## Contents

Abbreviations and Acronyms .....	vi
Overview.....	viii
The Report Card: Goals and Targets from the Millennium Declaration.....	1
Eradicating extreme poverty and hunger .....	6
Achieve universal primary education .....	9
Promote gender equity and empower women .....	12
Reduce child mortality.....	14
Reduce maternal mortality.....	16
Combat HIV/AIDS, malaria, and other diseases .....	18
Ensure environmental sustainability.....	21
Develop a global partnership for development.....	23
Improving the measurement of development goals.....	25
1.    Macroeconomic, Trade, Aid Developments, and the Millennium Development Goals .....	27
Growth and macroeconomic adjustment in developing countries.....	27
A modest uptick in global economic growth to provide renewed support toward achieving the MDGs	28
Managing macroeconomic risks in low-income countries .....	41
Economic diversification and structural transformation.....	45
Update on trade trends and trade policy developments .....	54
Aid and international financial institutions.....	58
Bilateral and Multilateral Aid.....	58
Gleneagles .....	59
Regional aid.....	59
Special groups.....	60
BRICS.....	62

Aid effectiveness .....	63
Acceleration towards the MDGs .....	70
Improving the effectiveness of projects through the use of ICT .....	70
Chapter 1 References .....	74
Annex 1.1: Country Classifications in World Economic Outlook, 2013.....	76
2. Rural-Urban Disparities .....	77
Introduction .....	77
Why urbanization matters for the MDGs .....	79
The majority of the poor remain in rural areas .....	80
Urbanization often fuels prosperity and dampens poverty, but not always.....	82
Poverty is located along a “rural” to “urban” spectrum.....	83
Unveiling the face of urban poverty – cities and small towns.....	86
Linkages between urbanization and rural poverty.....	90
Urban growth can reduce rural poverty through rural–urban migration.....	91
Non-farm employment and rural poverty .....	96
Urbanization and delivery of MDG-related services.....	97
Access to primary education affects achievement of prosperity .....	98
Rural-urban differentials in health indicators .....	104
Urbanization, congestion, and slums .....	112
Policy challenges and implications.....	120
Chapter 2 References .....	123
Annex 2.1: Equalization of Health Service Delivery and Their Expected Impacts on the MDGs: A Simulation Exercise .....	130
3. How Can Urbanization Accelerate Progress Towards the MDGs?.....	136
Summary and messages.....	136

Framework for urbanization policy .....	139
Planning cities.....	142
Connecting cities .....	158
Financing cities.....	162
Going forward: addressing the MDG challenge from subnational levels—three priorities .....	171
Planning first, followed by financing .....	174
Chapter 3 References .....	178
Annex 3.1: International Financial Institutions and Urbanization .....	181

## List of Boxes

Box 1: The MDG for Extreme Poverty.....	xi
Box 1.1: Operationalizing the Busan Partnership for Effective Development Co-operation .....	65
Box 1.2: World Bank Performance on Development Cooperation.....	67
Box 1.3: Potential Uses of Mobile Phone Surveys .....	73
Box 2.1: Is the Policy Agenda Different for Leading-Lagging Regions? The Case of Uganda.....	95
Box 2.2: Leveraging the Private Sector to Reach the Health-Related MDGs .....	107
Box 2.3: Water in Africa: Sustainable PPPs in Rural and Small Towns - Strong Public Sector Leadership is Key .....	111
Box 2.4: Costs of Coping with Lack of Water Service Provision .....	115
Box 2.5: Agglomeration of Collective Capacity among Uganda’s Slum Dweller Communities.....	118
Box 2.6: Catalyzing Citywide Development through Toilet Design in the Slums of Agra, India .....	119
Box 3.1: Bangalore Has Nurtured Skills – But Must Now Tackle Infrastructure .....	139
Box 3.2: Do Cities Need Master Plans?.....	148
Box 3.3: Publicly Accessible Information on Urban Hazard Risk Can Improve Household Decision Making.....	149
Box 3.4: A Tale of Two Sectors – Expanding Access to Services .....	153
Box 3.5: Using Output-Based Aid in Urban Projects .....	157
Box 3.6: Pricing and Funding Through Ancillary Services.....	162
Box 3.7: Key Design Issues of Decentralization .....	166
Box 3.8: The Complex Structure of Metropolitan Governments.....	170
Box 3.9: Learning from Urbanization in the BRICS .....	176

## List of Figures

Figure 1: Global progress toward achievement of the MDGs .....	x
Figure 2: Number of countries making progress toward various MDGs.....	xii
Figure 3: Shanghai’s spatial expansion as evidenced by average nighttime light intensity.....	xx
Figure 1.1: GDP per capita growth .....	30
Figure 1.2: Global current account imbalances .....	32

Figure 1.3: Low-income countries: imports, exports, and current account balance including FDI.....	34
Figure 1.4: Official reserves .....	34
Figure 1.5: Commodity price indexes.....	35
Figure 1.6: Changes in commodity prices and changes in GDP per capita, TOT and inflation .....	35
Figure 1.7: Fiscal deficit .....	37
Figure 1.8: Monetary policy loosening .....	38
Figure 1.9: Average year-on-year growth in money and the money-gap in emerging market countries .....	38
Figure 1.10: Macroeconomic policy mix .....	39
Figure 1.11: Quality of macroeconomic policies in low-income countries .....	40
Figure 1.12: Selected macroeconomic indicators for Low-Income Countries – 2007-2013 .....	42
Figure 1.13: Low-Income Countries - impact of a protracted slowdown in global growth.....	43
Figure 1.14: Agglomeration and income distribution, 2010 .....	46
Figure 1.15: Diversification spurts and growth accelerations.....	50
Figure 1.16: Sub-Saharan Africa: Sectoral output and employment, 1995-2010 .....	52
Figure 1.17: Sub-Saharan Africa - Labor productivity and change in employment shares, 1995-2010.....	53
Figure 1.18: South East Asia - labor productivity and change in employment shares, 1995-2010 .....	53
Figure 1.19: Trade developments since 2008 .....	55
Figure 1.20: G20's new trade restrictive measures.....	56
Figure 1.21: Total number of measures implemented and still in force by each G20 country November 2008 - December 2012.....	57
Figure 1.22: DAC members' net ODA disbursements .....	58
Figure 1.23: Net ODA disbursements to developing regions .....	60
Figure 1.24: Net ODA disbursements to low- and middle-income countries.....	60
Figure 1.25: Net ODA disbursements to fragile, small, and HIPC states .....	61
Figure 1.26: Net ODA received per capita by groups of countries ranked by MDG targets met or on track to be met by 2015.....	62
Figure 1.27: Net ODA received per capita by groups of countries ranked by MDG targets met or on track to be met by 2015 (2009-2011).....	62
Figure 2.1: Urbanization is occurring faster in developing countries than in the rest of the world .....	77
Figure 2.2: Overall poverty has declined .....	79
Figure 2.3: Nexus between urbanization, poverty, and prosperity .....	82
Figure 2.4: Poverty is located along a rural-urban spectrum .....	83
Figure 2.5: Proportion of urban population living in slums, 1990-2010.....	85
Figure 2.6: In India and Vietnam, poverty in small towns is worse than in large cities .....	89
Figure 2.7: Population in rural areas and employment in agriculture.....	90
Figure 2.8: Travel time to cities in Nepal .....	93
Figure 2.9: In SSA, primary school enrollment remains low .....	99
Figure 2.10: Rural–urban differences in primary school completion rates in India.....	101
Figure 2.11: Literacy rates in rural areas and smaller towns are worse than in large cities.....	103
Figure 2.12: Rural-urban differentials in infant mortality rates remain huge .....	105
Figure 2.13: Rural-urban differentials in the delivery of health care are huge in SSA.....	106
Figure 2.14: Within countries, access to sanitation is better in urban areas even in the most urbanized countries (share of population with access (%)) .....	108
Figure 2.15: Small towns have poorer service delivery than large cities.....	109

Figure 2.16: Access to safe water is nearly equal in rural and urban areas of SSA and South Asia .....	109
Figure 2.17: Slums decline as countries become better at managing them.....	113
Figure 3.1: Shanghai’s spatial expansion as evidenced by average nighttime light intensity.....	137
Figure 3.2: A framework for urbanization policy: planning, connecting, and financing.....	141
Figure 3.3: Vietnam’s dual land price system creates problems for the assembly of large plots of land needed for industry .....	143
Figure 3.4: New York’s density management is granular and integrated with infrastructure while Mumbai’s is coarse and not integrated .....	147
Figure 3.5: Share of population with access to piped water by country and across city size .....	151
Figure 3.6: Ratio of public transit fares to operating costs in a selection of the world’s largest cities.....	158
Figure 3.7: Costs of moving freight in India.....	159
Figure 3.8: Modes of transport to work in Uganda’s urban areas (%).....	161

## List of Maps

Map 2.1: The poor are mostly concentrated in less urbanized countries .....	78
Map 2.2: The poor are also concentrated in less urbanized regions .....	78
Map 2.3: Regional differences in access to sanitation are highest in the least urbanized regions (urban-rural differentials (%)) .....	81
Map 2.4: The gap between urbanization levels in low- and high-income countries in 1990 was large.....	84
Map 2.5: Progress in developing countries, especially East Asia, in narrowing the gap in urbanization with high-income countries in 2010.....	84

## List of Tables

Table 1: Poverty is decreasing in both urban and rural areas but urban areas have less poverty .....	xv
Table 1.1: Global output .....	29
Table 1.2: Government revenue excluding grants .....	31
Table 1.3: Net financial flows.....	33
Table 1.4: IMF and World Bank member countries: selected indicators, 2010.....	47
Table 1.5: Average real GDP per capita growth, 2003-12.....	48
Table 1.6: Statistical tests for mean-differences .....	49
Table 1.7: Progress on Paris Declaration survey indicators by multilateral development banks, UN, and EU institutions .....	69
Table 1.8: Mobile technology and the Millennium Development Goals.....	71
Table 2.1: Rural and urban poverty is declining in developing countries.....	80
Table 2.2: The primacy of smaller towns matters for urban poverty.....	86
Table 2.3: The poor are disproportionately concentrated in smaller cities and towns.....	87
Table 2.4: Educational attainment conditional on starting primary education .....	99
Table 2.5: Pupils’ achievement levels in reading and mathematics in SSA, 2007 .....	102
Table 2.6: Market share of public and private schools in Africa (%) .....	104
Table 2.7: Access to basic infrastructure services in SSA, 1990–2005 ( %).....	110

## Abbreviations and Acronyms

ADB	Asian Development Bank
ADF	African Development Fund
AfDB	African Development Bank
BRICS	Brazil, Russia, India, China and South Africa
CGE	computable general equilibrium
CPA	country programmable aid
CSO	civil society organization
DAC	Development Assistance Committee
DDA	Doha Development Agenda
DHS	Demographic and Health Surveys
DIME	Development Impact Evaluation Initiative
EAP	East Asia and Pacific
EBRD	European Bank for Reconstruction and Development
ECA	Europe and Central Asia
EU	European Union
FAO	Food and Agriculture Organization
FCS	fragile and conflict-affected states
FDI	foreign direct investment
FSI	floor space index
GCC	Gulf Cooperation Council
GDP	gross national product
GMR	Global Monitoring Report
GNI	gross national income
GPS	global positioning system
GTA	Global Trade Alert
HIPC	highly indebted poor countries
HIV/AIDS	human immunodeficiency virus / acquired immunodeficiency syndrome
IATI	International Aid Transparency Initiative
ICT	information and communications technology
ICTSD	International Centre for Trade and Sustainable Development
IDA	International Development Association
IDB	Inter-American Development Bank
IFC	International Finance Corporation
IMF	International Monetary Fund
LAC	Latin America and the Caribbean
LDC	least developed country
LIC	low-income country
MAF	MDG acceleration framework
MDB	Multilateral Development Banks
MDG	Millennium Development Goal
MDRI	Multilateral Debt Relief Initiative
MENA	Middle East and North Africa
MIC	middle-income country
NER	net enrollment rate
NGO	non-governmental organization
OBA	output-based aid

ODA	official development assistance
OECD	Organisation for Economic Co-operation and Development
PBIG	Post Busan Interim Group
PFM	public financial management
PISA	Program for International Student Assessment
PPP	public-private partnership
PPP	purchasing power parity
RMC	regional member countries
SACMEQ	Southern and Eastern Africa Consortium for Monitoring Educational Quality
SAR	South Asia
SMS	short message service
SNG	sub-national government
SSA	Sub-Saharan Africa
SST	small states
TIMSS	Trends in International Mathematics and Science Study
UN	United Nations
UNAIDS	Joint United Nations Programme on HIV/AIDS
UNDP	United Nations Development Programme
VT	<i>vale transporte</i>
WDI	World Development Indicators
WDR	World Development Report
WHO	World Health Organization
WP-EFF	Working Party on Aid Effectiveness
WTO	World Trade Organization

## Overview

The *Global Monitoring Report* (GMR), jointly produced by the World Bank and International Monetary Fund (IMF), is an annual report card on the world's progress towards the Millennium Development Goals (MDGs). Now in its 10<sup>th</sup> edition, the GMR also outlines prospects for the attainment of the MDGs and assesses the support of the international community. Achieving as many MDGs as possible before 2015 remains an urgent endeavor for the development community. This GMR highlights those MDGs that are lagging in progress and consequently need additional attention, while pointing out that accelerating towards attainment of one MDG will likely provide spillovers to the attainment of others. It shows that Official Development Assistance (ODA) and progress with aid effectiveness have been less than stellar.

Each year's report has a thematic focus, an aspect of the development agenda on which the GMR provides a more in-depth assessment. The theme of *GMR 2013* is rural-urban disparities in development and how urbanization can better help achieve the MDGs. The theme is not only highly relevant for assessing progress within the current MDG framework, but it also has the potential to inform discussions about the post-2015 development framework, as 96 percent of the additional 1.4 billion people in the developing world in 2030 will live in urban areas.

Urbanization matters. In the past two decades, developing countries have urbanized rapidly, with the number of people living in urban settlements rising from about 1.5 billion in 1990 to 3.6 billion (more than half of the world's population) in 2011. The report finds that urban poverty rates are significantly lower than rural poverty rates and that urban populations have far better access to the basic public services defined by the MDGs, such as access to safe water and sanitation facilities, even though within urban areas there are large asymmetries in access. If the forces of urbanization are not managed speedily and efficiently, slum growth can overwhelm city growth, exacerbate urban poverty, and derail MDG achievements. However, the GMR points out that people are located along a continuous rural-urban spectrum and that large cities are not necessarily places where the urban poor are concentrated. Smaller towns matter hugely for urban poverty reduction and service delivery. As urban centers continue their inexorable growth over the next two decades, *GMR 2013* calls for an integrated strategy to better manage the planning-connecting-financing formula of urbanization.

Notwithstanding the importance of urbanization in poverty reduction and MDG attainment, rural areas remain a huge challenge. This underscores the importance of being vigilant regarding policies that aim to improve agricultural productivity, which if successful provides positive synergies for farm incomes and non-farm employment. The 2012 Global Monitoring Report highlighted the promotion of increased yields through research, extension, and improved water management, improvements in the functioning of land markets, and increased integration of domestic markets with world markets as a possible set of policies that would positively contribute to increased productivity in the agricultural sector. With 75 percent of the world's poor residing in rural areas, the challenge of effective rural development remains daunting but achievable with complementary rural-urban development policies and actions.

## Progress toward Achieving the MDGs – The Report Card

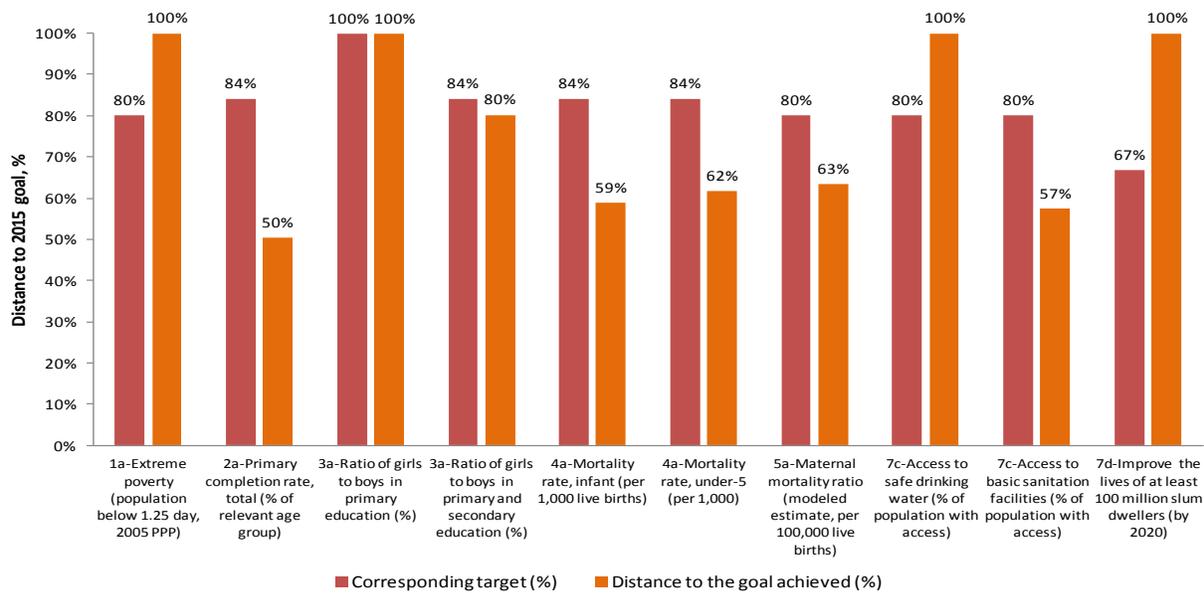
With the 2015 deadline set by the international development community to attain the MDGs just over two years away, only four of the 21 MDG targets or subtargets have been met worldwide (Figure 1). New estimates confirm last year's reports that MDG1.a was reached in 2010—the US\$1.25 a day poverty rate (2005 purchasing power parity) and had fallen below half of its 1990 value. As reported before, the world also met part of MDG7.c – to halve the proportion of people without safe access to drinking water – in 2010. MDG7.d – to have achieved a significant improvement in the lives of at least 100 million slum dwellers by 2020<sup>1</sup> – was also achieved. Finally, the first part of MDG3.a – to eliminate gender disparity in primary education – was accomplished in 2010. Global progress on the full MDG3.a (to eliminate gender disparity in primary and secondary education) is close to being on track.

Overall global progress on the remaining MDGs has been less than stellar, however, particularly on those related to education (MDG2.a) and health (MDG4.a and 5.a), and a vast acceleration of progress is needed to achieve all of the goals by 2015. Accelerating progress towards attainment of these MDGs is not only intrinsically desirable, but there are positive spillovers between attaining these different development objectives. Reducing infant mortality and improving maternal health can pay additional dividends by increasing the returns to subsequent investments in human capital. There is a vast literature demonstrating that human capital formation is a cumulative process and that the first few years in a child's development are critical, as was pointed out in last year's GMR. For MDG2.a (ensuring that, by 2015, children everywhere will be able to complete a full course of primary schooling), it might be too late, as completion rates depend on net enrollment rates and those have not reached 100 percent: in 2011, the net enrollment rate in primary education stood at only 88.8 percent globally.

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<sup>1</sup> The original target to improve the lives of at least 100 million slum dwellers by 2020 was based on an estimation of close to 100 million slum dwellers in the world. Upon measurement of slum population using the internationally agreed upon UN-Habitat definition of slums following the UN Expert Group Meeting of October 2002, it was learnt that the global estimate of slum population was in fact close to one billion mark (924 million). As a result, even though the slum target has been globally achieved, and in fact significantly surpassed 10 years ahead of schedule, there is little room for complacency given the existing magnitude of populations currently living in slums.

**Figure 1: Global progress toward achievement of the MDGs**



Developing countries, percent of total required progress between 1990 and 2015, as achieved in 2011 or 2010.

*Note:* Intermediate target calculated using a linear progression over 25 years, resulting in a needed progress of 4 percent per annum. Note that the corresponding target for 2010 would equal 80 percent, and for 2011, 84 percent, to be on track to attain the MDG by 2015. Any value above those intermediate targets indicates that the world is ahead of the required pace to meet the MDG. A value of 100 percent means that the MDG has been met.

*Source:* World Bank staff estimates.

Regional progress towards achieving the MDGs is more diverse. At one end of the spectrum, the East Asia and Pacific region is on target to meet most of the MDGs except for MDG2.a (primary completion rate), while at the other end, Sub-Saharan Africa (SSA) is off target regarding most of its MDGs. It should be noted, though, that those regions still lagging also required the most absolute progress given their initial starting positions and have made significant progress in absolute terms, particular in those MDGs that the world as a whole is struggling to meet. The relative nature by which many of the MDGs are defined masks to a large extent these accomplishments. Evaluating progress towards attainment of the MDGs at the country level shows even further diversity (Figure 2). Sufficient progress towards MDG3.a is most prevalent, with 72 countries on track, while only 18 countries are on track to meet MDG4.a (reducing infant mortality). However, an additional 20 countries are anticipated to meet this MDG between 2015 and 2020. With a significant acceleration of effort, these countries could achieve MDG4.a by 2015 or shortly thereafter. The same holds for the reduction in under-5 mortality: 22 countries have made progress but require an additional push to achieve the target by or close to 2015.

### Box 1: The MDG for Extreme Poverty

New poverty projections for 2015 are the result of various updates of new and more recent household surveys and a new forecast of per capita consumption growth. For close to 40 developing countries, sufficient data do not exist to estimate progress in extreme poverty. Consequently, the forecasts for these countries capture changes in income poverty in the surveys of other countries.

Based on updated economic projections of developing countries by the IMF and the World Bank, an estimated 962 million people in 2015 continue to live below US\$1.25 a day, equivalent to 15.4 percent of the population in the developing world. This is lower than the previous estimate of 1 billion people (16.3 percent) done in 2012. It is significantly lower than the 1.9 billion people living in extreme poverty in 1990 (43.1 percent).

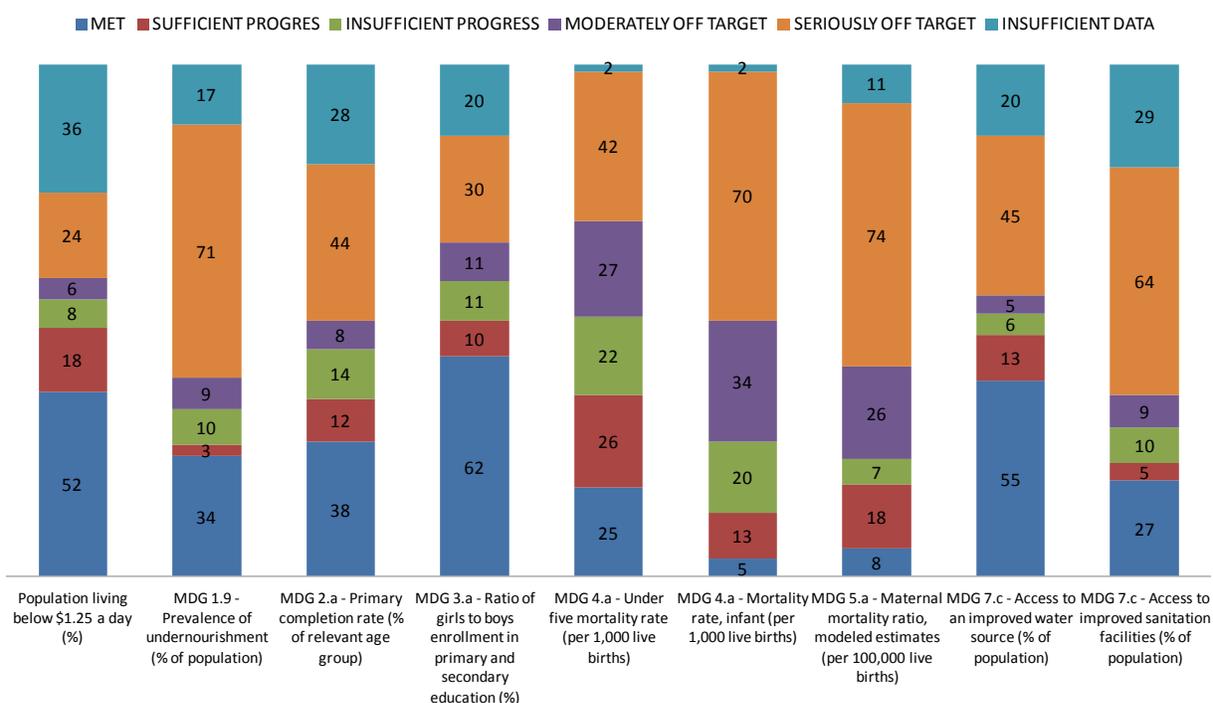
Except for Sub-Saharan Africa, which had the worst starting position, all regions are expected to achieve the MDG1.a target of halving extreme poverty by 2015.

**Box Table 1: Poverty by region**

<b>% of population below US\$1.25 a day (2005 PPP)</b>				
<b>Region</b>	<b>1990</b>	<b>2005</b>	<b>2008</b>	<b>2015 (forecast)</b>
East Asia and Pacific	56.2	16.8	14.3	5.9
Eastern Europe and Central Asia	1.9	1.3	0.5	0.2
Latin America and the Caribbean	12.2	8.7	6.5	4.9
Middle East and North Africa	5.8	3.5	2.7	2.5
South Asia	53.8	39.4	36.0	23.3
Sub-Saharan Africa	56.5	52.3	47.5	40.9
<b>Total</b>	<b>43.1</b>	<b>25.0</b>	<b>22.4</b>	<b>15.4</b>
<b>Millions of people below US\$1.25 a day (2005 PPP)</b>				
<b>Region</b>	<b>1990</b>	<b>2005</b>	<b>2008</b>	<b>2015</b>
East Asia and Pacific	926.4	332.1	284.4	121.2
Eastern Europe and Central Asia	8.9	6.3	2.2	1.1
Latin America and the Caribbean	53.4	47.6	36.8	30.0
Middle East and North Africa	13.0	10.5	8.6	8.8
South Asia	617.3	598.3	570.9	407.2
Sub-Saharan Africa	289.7	394.9	386.0	393.8
<b>Total</b>	<b>1,908.6</b>	<b>1,389.6</b>	<b>1,289.0</b>	<b>962.1</b>

Source: World Bank staff calculations from PovcalNet database. See <http://iresearch.worldbank.org/PovcalNet/index.htm> for additional information and data.

**Figure 2: Number of countries making progress toward various MDGs**



*Note:* Progress is based on extrapolation of the latest five-year annual growth rates for each country, except for MDG5, which uses the last seven years. Sufficient progress indicates that an extrapolation of the last observed data point with the growth rate over the last observable five-year period shows that the MDG can be attained. Insufficient progress is defined as being able to meet the MDG between 2016 and 2020. Moderately off target indicates that the MDG can be met between 2020 and 2030. Seriously off target indicates that the MDG will not even be met by 2030. Insufficient data points to the fact that not enough data points are available to estimate progress or that the MDG's starting value is missing (except for MDG2 and MDG3).  
*Source:* WDI and GMR team estimates.

## Macroeconomic Challenges, Aid Flows, and Aid Effectiveness

### Global growth and its implications for the MDGs

The global economy is expected to recover, but only very gradually, during 2013. While the road to recovery in advanced economies will remain bumpy, downside risks to the outlook have eased as policy intentions in advanced economies have become clearer and commodity price volatility has abated. While important short- and medium-term downside risks remain—including adjustment fatigue in advanced economies and overinvestment and high asset prices in emerging market and developing countries—overall risks are now more symmetric. A broadly appropriate current policy stance in emerging market and developing countries is supporting continued strong growth in these countries. Commodity prices trended down through most of 2012 and are expected to remain weaker in 2013, providing room for a flexible implementation of monetary policy, particularly in emerging market and developing countries.

The downside risk of a protracted global growth slow-down extending through 2015 would have a significantly negative impact on growth in low-income countries and their ability to attain the MDGs. Despite sustained economic growth, progress in rebuilding policy buffers in low-income countries has been modest. Indeed, with policy buffers not yet restored to levels preceding the 2009 crisis and against the backdrop of reduced traditional sources of financing, most low-income countries would likely need to undertake adjustments in the face of such a shock. There are large differences across countries, however.

Still high international commodity prices are providing commodity exporters with relatively larger buffers than commodity importing countries.

### **Aid flows and its effectiveness**

The international development finance architecture has changed markedly since the Millennium Declaration in 2000. In particular, the relative importance of ODA as a financing instrument for development has declined. The main drivers of that change are the increasing role of developing countries in the global economy, with a massive expansion of net private flows to those countries, and the emergence of middle-income countries as growth poles and important sources of non-ODA development finance.

Even though tough economic challenges have emerged in the developed world over the last few years, it is important that OECD Development Assistance Committee (DAC) donors live up to earlier promises to maintain and expand aid flows and improve their aid effectiveness to strengthen the impact of the promised aid. Especially when the size of ODA flows relative to other financial flows is declining, the quality of aid flows and changes in the effectiveness of domestic policies that it can support become paramount. With improved policies in developing countries, the potential effectiveness of aid has increased. But if this potential is to be fully exploited, donors will have to follow up on aid effectiveness agreements and deliver on their pledges.

At the Gleneagles summit in 2005, DAC donors agreed to increase ODA by US\$50 billion between 2004 and 2010, with at least half of the increase designated for Africa; both Sub-Saharan Africa and North Africa. The promised increase of US\$50 billion made in 2004 prices and exchange rates would equal an increase in ODA to a level of US\$152.2 billion in 2010 prices and exchange rates. In reality, disbursements were only US\$128.5 billion in 2010, leaving a gap between initial pledges and actual disbursements of over US\$25 billion. Africa received an additional US\$11.8 billion, well short of the pledged US\$25 billion. In its 2012 annual ODA report, the DAC estimated that only about US\$1.2 billion of the shortfall could be attributed to lower than expected gross national income levels due to the recent global economic crisis.

Improving aid effectiveness could make up for some of the shortfalls, but bilateral and multilateral DAC donors have been unable to reach the ambitious targets set out in the Paris Declaration on Aid Effectiveness. Collectively, the multilateral development banks have reached only one target out of the 13 established in Paris (i.e., to strengthen capacity by coordinated support). Disaggregating the data by the various multilateral development banks and other international organizations such as the United Nations (UN), and the European Union (EU) institutions yields a more nuanced picture. For example, the Inter-American Development Bank (IDB) has met four out of the eight indicators for which disaggregated data exist, the World Bank three, and the EU institutions two. All other multilateral development banks have met one indicator.<sup>2</sup>

The new Global Partnership for Effective Development, agreed upon in the Fourth High Level Forum on Aid Effectiveness in Busan in 2011, represents a window of opportunity for a more balanced international dialogue among all development partners, including traditional DAC and non-DAC donors such as the

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<sup>2</sup> As detailed in the OECD's report "Aid Effectiveness 2005-10: Progress in Implementing the Paris Declaration" (2012).

BRICS. The Partnership provides space for these partners to agree on more realistic targets for aid effectiveness and to establish mutual accountability to implement agreed-upon actions. To date, over 160 countries and 45 organizations from around the world have endorsed the Partnership.

Notwithstanding these emerging trends in development finance and the aid effectiveness of DAC donors, development partners, including international financial institutions, continue to play an important role in assisting developing countries to implement policies and programs that help improve progress on the MDGs and other development outcomes. These knowledge transfer activities, including South-South learning, have the potential to grow into effective partnerships with strong country ownership.

## Rural-Urban Disparities, Urbanization, and the MDGs

Economic aspects of agglomeration are most often looked at from a microeconomic perspective, but broad-based changes to where people work and live obviously also have profound macroeconomic consequences; for example, with regard to economic structural changes. Using an agglomeration index developed for the *2009 World Development Report on Economic Geography*,<sup>3</sup> evidence suggests that there are relatively higher returns to agglomeration on the lower rungs of development. Recent research at the IMF suggests that greater economic diversification is associated with improved macroeconomic performance. Another strand of research that has benchmarked Africa's structural transformation with that of Asia's provides some optimism with regard to Africa's economic prospects.

Cities and towns are the hubs of prosperity – over 80 percent of global economic activity is produced in cities by just over half of the world's population. Economic agglomeration increases productivity, which in turn attracts more firms and creates better paying jobs. Urbanization provides higher incomes for workers than they would earn on a farm, and it generates further opportunities to move up the income ladder. Between 1990 and 2008, rural poverty rates were without exception higher than urban poverty rates (Table 1). Indeed, more urbanized countries have had greater success in attaining the MDGs than less urbanized ones: countries with a degree of urbanization of over 60 percent are expected to achieve 50 percent more of the MDGs than those with a degree of urbanization of 40 percent or less.

Urban poverty rates have not only been relatively low, but have also declined in all regions between 1990 and 2008. In the process, rural poverty rates have also declined, as autonomous productivity increases in agriculture have increased rural incomes, and because urbanization has created new opportunities in rural areas. East Asia's success in urban and rural poverty reduction has been spectacular, driven to a large extent by China's achievement. East Asia had in 1980 a level of urbanization similar to South Asia and Sub-Saharan Africa, but had the highest poverty rate of all regions. Its success in poverty reduction over the last three decades was linked to its rapid urbanization rate, which more than doubled from 21.5 percent in 1980 to 49 percent in 2010. In 1980, South Asia's and Sub-Saharan Africa's urbanization rates were slightly above East Asia's, but they had increased to only 37 percent by 2010. It is important to

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<sup>3</sup> Many reasons for the occurrence of urbanization were discussed in the *2009 World Development Report*, which provided ample evidence of the benefits of agglomeration. The 2009 WDR developed an agglomeration index to come to a uniform definition of what constitutes an "urban" or agglomerated area. It combines information about population size of a settlement (> 50,000), population density (> 150 people per square kilometer), and travel time to the nearest large city (60 minutes travel time).

realize, however, that urbanization by itself is no guarantee for success. If unregulated and poorly planned, rapid urbanization can lead to disproportionate increases in slums.

**Table 1: Poverty is decreasing in both urban and rural areas but urban areas have less poverty**

	Share of the population below \$1.25/day											
	1990			1996			2002			2008		
	rural	urban	total	rural	urban	total	rural	urban	total	rural	urban	total
East Asia & Pacific	67.5	24.4	54.9	45.9	13.0	34.6	39.2	6.9	26.3	20.4	4.3	12.9
Europe & Central Asia	2.2	0.9	1.4	6.3	2.8	4.1	4.4	1.1	2.3	1.2	0.2	0.6
Latin America & Caribbean	21.0	7.4	11.5	20.3	6.3	10.0	20.3	8.3	11.1	13.2	3.1	5.3
Middle East & North Africa	9.1	1.9	5.3	5.6	0.9	3.1	7.5	1.2	4.0	4.1	0.8	2.2
South Asia	50.5	40.1	47.9	46.1	35.2	43.2	45.1	35.2	42.3	38.0	29.7	35.5
Sub-Saharan Africa	55.0	41.5	51.3	56.8	40.6	51.9	52.3	41.4	48.7	45.7	33.6	41.5

Source: World Bank staff calculations.

The challenge of poverty reduction remains in rural areas, and is concentrated in Asia and Sub-Saharan Africa. In 2008, 46 percent of Sub-Saharan Africa's rural population but only 34 percent of its urban population lived on less than US\$1.25 a day. For every two poor persons in urban areas of Sub-Saharan Africa, there were five in rural areas. In South Asia, the share of the poor in the population was 38 percent in rural areas and 30 percent in urban areas in 2008. Three-quarters of the poor in South Asia live in rural areas. Even in East Asia, which has led the race to reduce poverty, the number of rural poor was five times higher than in urban areas in 2008.

### Services are also better in urban areas

Apart from creating better paying jobs, cities also make, through their density, public services more accessible. For example, on average it costs US\$0.70 to US\$0.80 per m<sup>3</sup> to provide piped water in urban areas versus US\$2 in sparsely populated areas. South Asia and Sub-Saharan Africa have the largest rural-urban disparities in all service delivery indicators. The poor often pay the highest price for the water they consume while having the lowest consumption levels. For example, in Niger, the average price per m<sup>3</sup> of water is CFAF 182 for piped water from a network, CFAF 534 from a public fountain, and CFAF 926 from a vendor. And poor access to basic infrastructure disproportionately affects rural women, as they perform most of the domestic chores and often walk long distances to reach clean water.

Even in the poorest of countries, people have higher expectations for service delivery in cities: that water will flow when a tap is turned on; that one will have access to a toilet; or that one will find a doctor when a child has malaria. In 2010, 96 percent of the urban population in developing countries had access to safe drinking water compared to 81 percent of the rural population. Disparities in access to basic sanitation were greater: 80 percent of urban residents versus 50 percent of rural residents had access to a toilet.

Schooling and health care can also be delivered with economies of scale in dense environments, close to where people actually live. Urban citizens in rich and poor countries have better access than rural citizens to basic services, including those associated with the attainment of the MDGs. Quite often, both access to and quality of services are better in urban areas.

While good outcomes in nutrition, health, and education are development goals in themselves, they also combine to form human skills and abilities that are strongly linked to productivity growth and poverty reduction. Rural children are disadvantaged because they have access to services of much lower quality

than do urban children. The inability to attract teachers to rural schools is only one of the reasons for the poor quality of schooling in rural areas.

### **The spectrum of urbanization is wide**

Along the spectrum from rural to urban lie many types of settlements that vary from small towns to small cities and peri-urban areas to large cities. In many middle-income countries, e.g., India and Vietnam, the urban population is concentrated in the largest cities, but the urban poor are dispersed along a continuum of medium, smaller, and extra small towns, underscoring the fact that urban poverty is not just a large-city phenomenon. Research in India, for example, indicates that while poverty is primarily a rural phenomenon at the aggregate level, urban poverty is becoming a larger problem. The poverty rate for rural areas in India was 28 percent in 2004-05, compared to 26 percent in urban areas. Among urban areas, poverty rates were highest in small towns (population less than 50,000), at 30 percent, versus 15 percent in large cities (population of 1 million or more). The urban spectrum is less pronounced in Sub-Saharan Africa, where many countries are small and sparsely populated and urbanization is still in its early stages. Hence, poverty there is more concentrated in capital cities.

Small rural towns often have high concentrations of poor people. In the effort to escape rural poverty, some poor want to migrate to cities but are reluctant to dispose of their rural assets. In Nepal, where poverty is extreme, migrants prefer not to migrate too far from their rural residence, but value proximity to paved roads and areas with higher housing premiums. Many want to maintain links with their farms, while others fear losing their land if they migrate too far. Remaining close to one's land is an important factor in migration in the absence of efficient land markets.

### **Well-designed urbanization is needed to achieve the MDGs**

As long as rural-urban disparities in income and service delivery persist, rural-to-urban migration will ensue. Nearly 50 percent of the population in developing countries was urban in 2011, compared to less than 30 percent in the 1980s. Urban dwellers are expected to double between 2000 and 2030, from 2 billion to 4 billion people, and the number of Chinese urban dwellers will increase from over 622 million today to over 1 billion in 2030. This trend is not unique to developing countries – today's high-income countries underwent the same transformation in the 20<sup>th</sup> century. In fact, virtually no country has graduated to a high-income status without urbanizing, and urbanization rates above 70 percent are typically found in high-income countries.

For every 10 people lifted out of poverty in the East Asia and Pacific region, two were facilitated due to the urbanization process alone. Even in SSA, half of the decline in poverty originated in urban areas and through the urbanization process. Looking at the impact of urbanization on service delivery provides even stronger evidence of the importance of the process of urbanization itself: close to 30 percent of the improvement in the MDG on sanitation is due to the process of urbanization, i.e., the migration of people and the expansion of urban areas.

Policies to foster migration are important to enable the poor to migrate from lagging to leading areas, and governments can help reduce rural poverty by making migration more efficient. Equipping a citizen with human capital assets while s/he is still in a rural area will increase the chance that her/his job search in the city is successful. Many developing countries have instituted land market policies in rural areas that discourage migration to urban areas. Restrictions in the land market are detrimental not only to

agricultural productivity growth but also hinder diversification into non-farm activities that have higher returns. They should be relaxed.

However important facilitating the urbanization process is, it is not enough for successful development. Governments must also improve access to basic services in rural areas to achieve development goals and they face important tradeoffs in doing so. Priorities are not easily set and financing local services is not straightforward. Moreover, governments must address the problem of slums in urban areas and mitigate the negative side-effects of urbanization in the form of pollution caused by congestion or urban sprawl. To benefit fully from urbanization, smart planning of existing and/or new urban areas is needed.

### **Provision of services in rural areas**

Even as numerous towns emerge in rural areas and many poor people migrate to cities to seek better jobs and services, the vast majority of the poor are unlikely to urbanize at once. The prevalence of a large majority of the poor in rural areas remains of great concern. Rural areas need focused policies that help raise farm productivity and, more importantly, connect rural villages to input and output markets. Diversification of employment into non-agricultural activities can also reduce rural poverty. Growth of non-farm activities is often driven by growth in agricultural productivity, at least at the initial stage. Roads and the provision of electricity are needed to improve connectivity to markets and increase agricultural productivity.

As far as the MDGs reflect the basic needs of all citizens (primary education, access to clean water and sanitation, gender equality), governments should aim to attain them fully in both urban and rural areas. However, given scarce resources, priorities must be set. Consequently, it is important that when allocating resources, decision makers take into account country-specific circumstances.

For example, if the prime source of urbanization is domestic migration, then a strategy that focuses on MDG-related services that are portable (such as health and education) and that facilitate the integration of migrants seeking better opportunities in cities might have a higher payoff than one that indiscriminately tries to equalize MDG-related services across urban and rural areas. Early investments in education and health in rural areas will prove useful to those who seek jobs in cities, but can also contribute to higher farm and non-farm incomes for those who never migrate. This seems particularly relevant for sparsely populated countries with both low urbanization and agglomeration rates, as in Sub-Saharan Africa.

If the prime source of urbanization is gradual thickening of population density, then the country-wide expansion of water and sanitation systems should get higher priority. This seems most relevant for countries with a low urbanization rate but an elevated level of agglomeration, as is the case in various countries in South Asia.

If people get stuck in rural towns, with little prospect of moving on, then policies should focus on improving connectivity with other urban centers. Poverty in rural towns is often high, and the quantity and quality of services there differ little from those in rural areas and lag behind those in more mature urban settlements. Measures to better connect the activities in those rural towns with economies of larger cities are then paramount.

In all cases, the challenges should not be underestimated. Many developing countries have been unable to provide a coordinated package of physical infrastructure and social services in rural areas. In part, this is because the financing of public goods in poor areas is a daunting task, on which more is said below.

### **New forms of service delivery are required in slums**

Although poverty rates in cities are relatively low and declining, poverty is in many countries increasingly becoming an urban phenomenon as more and more people live in cities. Slums are the urban face of poverty and emerge when cities are unable to meet the demand for basic services and unable to supply the expected jobs. A likely 1 billion people live in urban slums in developing countries, and their numbers are projected to grow by nearly 500 million between now and 2020. Slums are growing the fastest in Sub-Saharan Africa, South-Eastern Asia, and Western Asia. Currently, 62 percent of Africa's urban population lives in slums. Women and children bear a disproportionate burden of improper sanitation and poor health care in slums. The lack of urban planning by governments has implications for the urban poor, especially in Asia and Africa. Qualitative research, community level surveys, and studies by NGOs show that the actions taken by the urban poor in response to inadequate urban institutional support can produce severe indirect impacts.<sup>4</sup>

The absence of land tenure is a key factor. According to the UN's *MDG Report 2012*, slum evictions without due legal process are the most visible violation of housing rights confronted by urban poor. Household surveys carried out in a range of cities globally found that in the majority of cities surveyed, slum dwellers' reported insecurity regarding possible eviction was high, ranging from 20 percent in Sao Paolo to nearly 45 percent in Lagos. Insecure tenure in slum settlements means that governments are unwilling or unable to provide basic services to these areas. In the absence of basic services, one coping strategy for the urban poor is dependence on informal providers, who offer low quality services, often at higher costs than those paid by the non-poor with access to formal services. This not only places higher economic costs on the urban poor but also leads to increased health costs, especially in the form of child morbidity from unclean water. Similarly, the lack of adequate sanitation facilities in low-income settlements can lower the school attendance of adolescent girls and eventually increase their dropout rates. This problem has been specifically detected in Kenya's urban slums, where qualitative and quantitative data show that girls in grades 4-8 who have reached puberty miss six learning weeks per year on average.

Combined with their informal employment, the inability of migrants to prove urban residence via water or electricity bills or formal rental leases in slums puts them in an even more precarious situation. In some countries, proof of urban residence is needed to access basic services, as is the case with health services in Kyrgyzstan. This can sometimes lead to reverse migration; for example, when the quality of health services is dismal or when a migrant is excluded due to lack of required documentation, an illness can push a migrant back to a rural area. Additionally, the inability to provide required identification and proof

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<sup>4</sup> The report draws upon an in-house desktop review of qualitative research, the findings of community-level surveys on slum dwellers in cities of developing countries, and fresh inputs sought from civil society organizations across a range of developing countries. This body of research has explored a range of themes affecting the urban poor, especially rural-urban migrants, and the strategies they apply to remain resilient to the challenges posed by urban poverty. Data and insights have been drawn from countries in Asia, SUB-SAHARAN AFRICA, and Latin America, including Bangladesh, India, China, Uganda, Kenya, Indonesia, Brazil, South Africa, Ghana, Zambia, Tanzania, Kyrgyzstan, Thailand, and Ecuador.

of urban residence excludes the urban poor from accessing financial services, leaving them with little means of saving for future investment or insurance in the event of economic shocks. In a detailed qualitative study of 176 rickshaw pullers in Delhi, only 1 percent had bank accounts although 95 percent consciously saved daily or periodically.

The most common coping strategies for saving in the absence of bank accounts include: depositing the money with a local shopkeeper or a relative/friend (with the risk of being cheated); carrying savings on one's person at all times; and burying small amounts in the ground or hiding money in perceived safe spots within one's residence. These invariably make the savings of the urban poor vulnerable to theft and destruction by pests or weather conditions. In the event of economic shocks from periods of unemployment or illness, the absence of savings can lead to discontinuation of children's education, especially that of girls, and to interruption in remittances. Remittances are also affected by the high cost of sending money by informal means, given the lack of access to banking by both the urban and rural poor.

Impermanent, unsafe housing and the lack of basic services in slums force some migrants to maintain split households (separating spouses and leaving children with grandparents in rural areas), thus introducing instability into the urban transition. This continued dependence on rural areas has several negative implications, including the increased burden of child care on aging grandparents, the inability of migrants' children to access better quality primary education and health services, and numerous other negative psychological and health consequences. Several studies from Asia and Sub-Saharan Africa have documented the effects arising from split households.

The key message is that governments should not discriminate between slum dwellers and the rural or urban poor. Slum dwellers should be provided access to basic services just like the poor in rural areas or cities, though the modalities may be different. Where land tenure issues are pervasive, such that services cannot be or are not connected to informal dwellings, public connections may be more appropriate. Alongside increased instances of slum evictions and slum clearance in the last decade, a growing number of success stories of slum service provision and *in situ* upgradation are beginning to get noticed. For example, in Lao PDR, the government had never previously given land on a long-term lease to a low-income squatter community; two recent projects in Lao are the first instances of the government doing this, thus regularizing people's status on public land they already occupied. Another way in which governments have contributed is by adjusting existing planning standards to make them more realistic, to lower costs, and to make it easier for the urban poor to develop housing that matches their needs, such as in the case of Vinh, Vietnam.

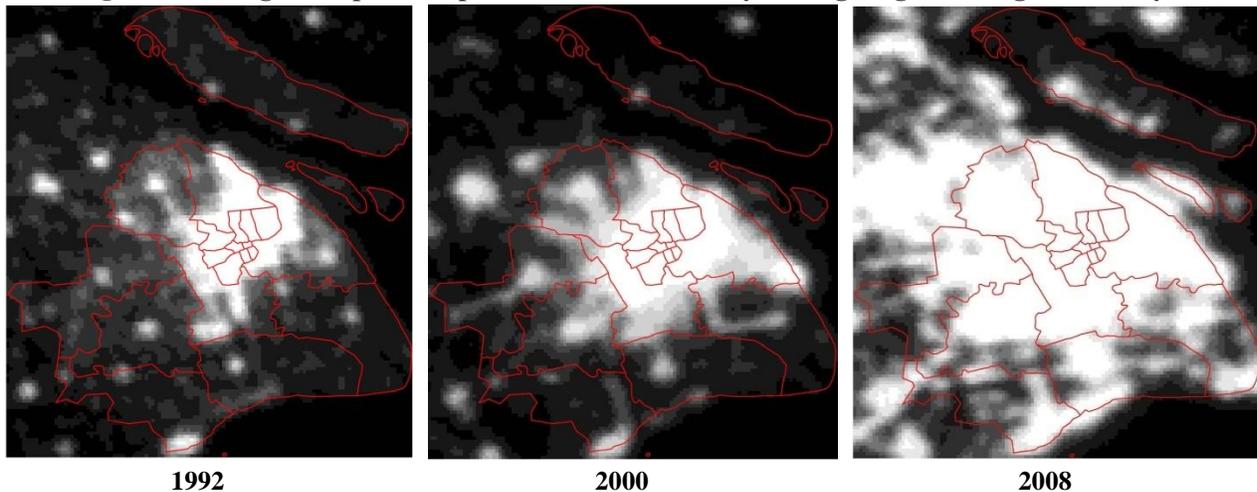
### **Uncoordinated urbanization can lead to pollution, sprawl, and congestion**

Urbanization is largely a natural process, driven by the opportunities cities offer. However, unregulated markets are unlikely to get densities right, and spontaneous development of cities can create negative side-effects in the form of congestion or, alternatively, excessive sprawl. The consequences are pollution and inefficiencies. Without coordinated actions cities will lack the proper investments to benefit from externalities generated by increased density. Supporting greater densities requires higher quality construction material and more sophisticated buildings. If these higher costs are fully internalized by firms and households, underinvestment is the result. In addition, complementary physical infrastructure is critical: roads, drainage, street lighting, electricity, water, and sewerage, together with policing, waste

disposal, and health care. While a market-driven process could possibly gradually increase densities via land values over time, the long-lived and lumpy nature of urban investment often inhibits such a process. A city's physical structures, once established, may remain in place for more than 150 years.

Under current trends, the doubling of the urban population in the developing world will be accompanied by a tripling in the built-up area of cities, from 200,000 to 600,000 square kilometers. As an example, consider Shanghai, which has rapidly expanded over the past 20 years (Figure 3). Such rapid population growth accompanied by an even faster spatial expansion of cities is likely to lead to low density development dominated by individual-vehicle transportation – a largely irreversible pattern. This will run the risk of dampening density-induced productivity and service delivery efficiencies. An additional consequence of rapid urban growth is worsening air quality; a recent study of the 189 largest cities using satellite data found that air quality worsened between 2002 and 2010, particularly in the largest cities of the Indian subcontinent, parts of Africa, the Middle East, and North China – places experiencing rapid urban growth.

**Figure 3: Shanghai's spatial expansion as evidenced by average nighttime light intensity**



*Source:* China Data Center at University of Michigan.

Emissions from fossil fuel burning include fine particulate matter (PM10 and PM2.5), carbon monoxide, nitric oxides, and sulfur dioxide, which can cause allergies, respiratory problems, cardiovascular disease, and cognitive deficits. The impacts are significant. In Russia, a conservative estimate suggests that annual health damages from fossil fuel burning amount to US\$6 billion. The social cost of transport in Beijing is equivalent to about 7.5-15 percent of its GDP, with about half of that stemming from air pollution. The largest share of these costs comes from increased mortality.

Globally, acute respiratory infections associated with air pollution cause about 20 percent of all under-5 mortality. In the FYRO Macedonia, a country of about 2 million people, an estimated 1,300 premature deaths are caused by air pollution. Dhaka, Beijing, Karachi, Cairo, and Delhi see an estimated 3,500 to 7,000 premature deaths annually from cardiovascular disease due to air pollution. Managing environmental quality while enhancing urban productivity is critical.

## An Integrated Strategy

Three interrelated dimensions of urban development triangulate the coordinated approach needed to enable a country to take advantage of its urbanization process: planning, connecting, and financing.

- *Planning* – charting a course for cities by setting the terms of urbanization, especially policies for using urban land and expanding basic infrastructure and public services.
- *Connecting* – making a city’s markets (labor, goods, and services) accessible to other cities and to other neighborhoods in the city, as well as to outside export markets.
- *Financing* – finding sources for large capital outlays needed to provide infrastructure and services as cities grow and urbanization picks up speed.

These are terms that policy makers use on a daily basis, but they often focus on financing first without fully considering the other two dimensions. Of the three, planning for land use and basic services is the most important. In fact, the key challenge for countries at all stages of urbanization is strengthening the institutions for land management. Yet because planning must allow for people and products to be mobile, it must be coordinated with connecting at all stages of a city’s growth. Financing should be city leaders’ last concern rather than their first.

### Urbanization should start with planning

Planning is fundamental to agglomeration economies in three ways. First, land use requires effective systems for land valuation. Second, land use must be allocated in a way that allows for infrastructure improvements as the city grows. Third, the most basic infrastructure services – water, energy, sanitation, and solid waste management – need to be provided for all residents, urban, peri-urban, and rural alike; natural market mechanisms are unlikely to provide those.

Lack of early planning often imposes very difficult corrective measures later on. These measures could have worked well at an early stage, but are much less effective once city structures have been locked in. For example, to manage slum formation and reduce the hazards faced by slum dwellers, policy makers often try to move people to safe environments or provide better housing elsewhere. Initiatives include: urban upgrades, such as community and household infrastructure projects; resettlement to new housing developments; housing subsidies; and land titling. But many of these policies do not work as people do not always willingly trade a better location for a better home with more modern utilities. People choose neighborhoods for their affordable services and amenities—but also for their proximity to jobs.

In many developing countries’ cities, it can be difficult to live near one’s job. One consequence of failed land markets and restrictive regulations is that the formal housing supply is low. But it may also be difficult and costly to commute to work, because transport infrastructure fails to connect urban neighborhoods. In many African cities, commuting by public transit costs more than half of a poor household’s income. In Harare, Zimbabwe, the poor spend more than a fourth of their disposable income on transport. In Kampala, Uganda, the figure is 50 percent.

To foster better living conditions, policy makers need to coordinate land market rules with urban infrastructure development. Hanoi has been able to grow without the formation of large slums because the government set prudent rules for land markets and infrastructure. It allowed the densification of former village areas. It pushed to modernize road networks just outside the city, yet it mostly avoided

demolishing older houses. These roads have opened new land for formal developers while improving connections between existing village areas and the city. The village areas were allowed to grow and were integrated into the urban economy.

Policy makers in Bogotá similarly succeeded by coordinating land use with infrastructure development. The Programa de Mejoramiento Integral de Barrios (PMIB) aimed to improve mobility and living conditions in 26 of the poorest city areas, called Unidades de Planificación Zonal. The Unidades comprised 107 neighborhoods of informal origin, with 1,440 informal settlements, 300,000 plots not formally titled, and about a half million structurally substandard dwellings. The PMIB legalized homes and neighborhoods; it expanded infrastructure with roads, rainwater traps, and sanitary and aqueduct trunk networks; and it added urban facilities (stairs, parks, community rooms). Living conditions improved for about 650,000 people.

Korea encouraged the development of a cadre of property appraisers during the 1970s. This has to be combined with the development of reliable and affordable public transit system to increase the effective distance that a worker can travel to access job opportunities. Complementary improvements in communication and interregional transport can make it easier to integrate neighboring rural areas with urban economies.

Integrating planning, connecting, and financing is also key to the “greening” of growth and getting urbanization right. While there is a perceived tradeoff between “building more cities” to accommodate rapid urban growth and “building cities right” to enhance social and environmental outcomes, there is compelling evidence showing that “building cities right” generates co-benefits in the near term and reduces the prohibitive costs of addressing sprawl, congestion, pollution, and climate change later. Integrating land use and transport plans effectively allows public transport (with its lower energy consumption and emissions) to be a major part of the modal structure in urban transport, provided in locations zoned for high density. In Brazil, the city of Curitiba has managed to concentrate its population around public transportation lines and hubs, making it possible to maximize the share of trips with low-energy consumption modes. And Copenhagen was designed following a transit-oriented and bike-friendly approach: it started with a “finger plan” – the identification of few priority development areas – and then invested in five-axis transit radials and corridors of new, satellite, rail-served towns.

### **Connectivity depends on more than infrastructure**

To benefit from the opportunities that cities offer, commuting costs need to be low. Moreover, if connections with the surrounding areas are well developed, urban densities can pull up also rural areas. In fact, research in India has shown a growing link between urban development and a reduction of rural poverty; higher demand for rural products and more options for rural non-farm diversification followed India’s economic liberalization in the early 1990s.

Connections – between and within cities – benefit producers and consumers, both in urban and rural areas. They give producers access to input (including labor) and output markets. They give consumers options and, in many cases, better prices. And connections expose cities and rural areas to new economic opportunities. But policy makers who envision better transport connections for cities and neighborhoods face difficult choices. With limited resources, they cannot invest in everything. It is hard to know which new or improved connections will yield the highest returns over time. Setting priorities for connective

investment means picking winners and losers in the short run – but in the long run, thinking about priorities can make a vast difference for cities, surrounding rural areas, and even countries.

More than building and fixing, efforts to improve intercity connections are about the economics of the transport sector, which has a tendency toward natural monopolies. If the market structure for transport service provision does not promote competitive pricing, any cost reductions stemming from network investments will be absorbed as profit by monopolistic providers. The government regulates in large part to induce healthy competition – limiting monopolistic behavior but also limiting the number or behavior of competitors where required. However, investments in infrastructure are more successful when bundled with regulatory reforms that promote competitive pricing while also ensuring compliance with safety standards.

In Uganda, as in many other African countries, a large gap between transport costs and prices attests to monopolistic behavior. Along the Kampala–Mombasa corridor, home to most of Uganda’s industrial production, transport prices are US\$2.22 per kilometer – double the average price in the United States – even though transport costs per kilometer are about US\$0.35 per kilometer. According to trucker surveys, 86 percent of the corridor is in good condition. So the fact that providers are making more than 85 percent profit suggests a need for competition, which can be most effectively induced through policy measures and regulation.

Within many cities, the poorest residents are often deprived of affordable transport services. An extreme example is Mumbai, where according to a study published in 2007, transport expenditure represented at least 16 percent of income for riders in the lowest income category – even though subsidies covered as much as 30 percent of transport costs. While subsidies have not always been successful, some targeted subsidies do reach the right groups and increase access to jobs. For example, South Africa uses highly subsidized weekly coupons – each for 10 journeys between black townships and industrial development areas – to connect low-income groups to jobs. And Brazil requires formal sector employers to provide transit tickets to employees through a system called *vale transporte* (VT); firms then deduct the VT expenditures from taxable income. The VT system – albeit affecting only the formal sector – effectively spreads the cost of transport subsidies between employers and the government.

### **Finance is the difficult final part of the puzzle**

Having identified priorities for planning and connecting, policy makers confront the problem of financing those investments. The main difficulty is the need for money up front. Large capital outlays are needed to provide infrastructure and services that are not fully in demand now, but will become so as urbanization picks up speed. The large capital investments that are needed in the construction phase – whether for transport, water provision, solid waste management, or sewage removal and treatment – are likely to far exceed the budget of any city government. But financing can become more sustainable through taxes realized with increased economic growth, and with the ability of policy makers to leverage land markets and approach local currency debt markets.

More generally, financing of all local services is challenging. While services are best delivered locally, the local tax base is often narrow. That is true not only for cities, but for all subnational governments

(SNGs).<sup>5</sup> SNGs are often better suited than higher levels of government to address the challenges of service delivery. First, they can more efficiently detect citizens' needs given their informational advantage. This is particularly relevant for beneficiary identification in poverty programs. SNGs can direct resources towards these needs (*allocative efficiency*) and can provide some services more efficiently than higher levels of government (*productive efficiency*). Decentralized management and execution of public investment can also be strengthened by joint approaches to address infrastructural gaps. Chile, for instance, is coordinating public investment through regional investment windows, including co-financing with municipalities. Also, political decentralization lowers the "barriers to entry" for different groups of society, so they can more easily and directly participate in decision making. An example from Mexico underscores the importance of decentralization: due to political resistance, federal teachers were not decentralized to the states, resulting in a parallel hiring process at the state level which blurred the lines of accountability.

Local provision of services requires fiscal equalization across space to ensure that required resources flow towards the districts most in need of them. The starting point is not a clean slate in any country, and more often than not, reforms of intergovernmental transfers are done at the margin and incrementally. This is exemplified by Colombia's current royalty reform, which achieves more equality for royalty resources.

The financing challenges are largest in rural areas: they host the largest number of poor people, but under growing disparities in fiscal capacity, they are increasingly resource constrained. SNGs in urban areas have higher fiscal capacity and are hence better able to influence outcomes through their own revenue decisions. Absent any convergence effects, fiscal capacity in urban areas will increase as agglomeration unfolds, putting rural areas at a further disadvantage. Given uneven advances and levels of autonomy in expenditures, rural SNGs are more constrained in their ability to provide a high quality package of services to the poor or to target the incidence of spending on direct services where they are needed most.

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<sup>5</sup> The term "subnational governments" encompasses, among other entities, regional or state governments, provinces, and municipalities.

## Issues for Discussion

The following issues are proposed for discussion by the Executive Directors

- How do directors assess the implications of rural-urban disparities for developing countries on growth, poverty reduction, and the MDGs? How do Directors assess the role of urbanization in achieving the MDGs?
- What do the Directors see as priorities for policy response in developing countries in addressing the challenges coming from urbanization and lagging rural areas?
- What do the Directors see as priorities for response by the international community on development assistance? What immediate actions are needed?
- What do Directors see as priorities for international financial institutions, especially the World Bank, in supporting countries in their efforts to manage urbanization? How could the World Bank group maximize its catalyst role in mobilizing support for urbanization and rural development?

# The Report Card: Goals and Targets from the Millennium Declaration

## 1 Eradicate extreme poverty and hunger

**TARGET 1.A** Halve, between 1990 and 2015, the proportion of people whose income is less than US\$1.25 a day.

**TARGET 1.B** Achieve full and productive employment and decent work for all, including women and young people.

**TARGET 1.C** Halve, between 1990 and 2015, the proportion of people who suffer from hunger.

## 2 Achieve universal primary education

**TARGET 2.A** Ensure that by 2015, children everywhere,

boys and girls alike, will be able to complete a full course of primary schooling.

## 3 Promote gender equality and empower women.

**TARGET 3.A** Eliminate gender disparity in primary and secondary education, preferably by 2005, and at all levels of education no later than 2015.

## 4 Reduce child mortality

**TARGET 4.A** Reduce by two-thirds, between 1990 and 2015, the under-5 mortality rate.

## 5 Improve maternal health

**TARGET 5.A** Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.

**TARGET 5.B** Achieve by 2015 universal access to reproductive health.

## 6 Combat HIV/AIDS, malaria, and other diseases

**TARGET 6.A** Have halted by 2015 and begun to reverse the spread of HIV/AIDS.

**TARGET 6.B** Achieve by 2010 universal access to treatment for HIV/AIDS for all those who need it.

**TARGET 6.C** Have halted by 2015 and begun to reverse the incidence of malaria and other major diseases.

## 7 Ensure environmental sustainability

**TARGET 7.A** Integrate the principles of sustainable development into country policies and programs and reverse the loss of environmental resources.

**TARGET 7.B** Reduce biodiversity loss, achieving



by 2010 a significant reduction in the rate of loss.

**TARGET 7.C** Halve by 2015 the proportion of people without sustainable access to safe drinking water and basic sanitation.

**TARGET 7.D** Have achieved a significant improvement by 2020 in the lives of at least 100 million slum dwellers.

## 8 Develop a global partnership for development

**TARGET 8.A** Develop further an open, rule-based, predictable, nondiscriminatory trading and financial system (including a commitment to good governance, development, and poverty reduction, nationally and internationally).

**TARGET 8.B** Address the special needs of the least-developed countries (including tariff-and quota-free access for exports of the least-developed countries; enhanced debt relief for heavily indebted poor countries and cancellation of official bilateral debt; and more generous official development assistance for countries committed to reducing poverty).

**TARGET 8.C** Address the special needs of landlocked

countries and small island developing states (through the Programme of Action for the Sustainable Development of Small Island

Developing States and the outcome of the 22<sup>nd</sup> special session of the General Assembly).

**TARGET 8.D** Deal comprehensively with the debt problems of developing countries through national and international measures to make debt sustainable in the long term.

**TARGET 8.E** In cooperation with pharmaceutical companies, provide access to affordable, essential drugs in developing countries.

**TARGET 8.F** In cooperation with the private sector, make available the benefits of new technologies, especially information and communications.<sup>6</sup>

<sup>6</sup> Source: United Nations. 2008. *Report of the Secretary-General on the Indicators for Monitoring the Millennium Development Goals*. E/CN.3/2008/29. New York.

Note: The Millennium Development Goals and targets come from the Millennium Declaration, signed by 189 countries, including 147 heads



of state and government, in September 2000 (<http://www.un.org/millennium/declaration/ares552e.htm>) and from further agreement by members states at the 2005 World Summit (Resolution adopted by the General Assembly—A/RES/60/1). The goals and targets are interrelated and should be seen as a whole. They represent a partnership between the developed countries and the developing countries “to create an environment—at the national and global levels alike—which is conducive to development and the elimination of poverty.”

# Progress towards the MDGs

With only two years left to reach the Millennium Development Goals (MDGs) in 2015, progress is diverse across targets and regions. Global estimates indicate that targets such as extreme poverty reduction (MDG 1.a), ratio of girls to boys in primary education (MDG 3.a), access to safe drinking water (MDG 7.c), and improving the lives of at least 100 million slum dwellers (MDG 7.d) have been reached (Figure 1). The proportion of people whose income is less than US\$1.25 a day fell from 43.1 percent in 1990 to below 21.5 percent in 2010, leaving 1.1 billion people in extreme poverty. The ratio of girls to boys in primary education was also accomplished in 2010. Similarly, the proportion of people without sustainable access to safe drinking water has already reached the goal.

On the other hand, progress on the remaining MDGs has been lagging, especially for education and health-related MDGs. Global targets related to infant and maternal mortality (MDGs 4.a and 5.a), and to a lesser extent, access to basic sanitation (MDG 7.c) are significantly behind and a vast acceleration of progress is needed to achieve all of the goals by 2015. Primary completion rate should have made 84 percent of progress by 2011, but this MDG has only made 50 percent of the progress needed. The infant and under-5 mortality rate, maternal mortality ratio, and access to basic sanitation targets are similarly behind.

Regionally, progress toward the MDGs is more diverse, although health-related targets will likely be missed in most regions (Figure 3). In East Asia and the Pacific, the targets on extreme poverty, gender parity, and access to water and sanitation have been reached. Although this region is close to reaching the primary education completion target, it has stagnated very close to

the goal. Under-5, infant and maternal mortality are the goals still lagging for East Asia and the Pacific.

Europe and Central Asia has made enough progress to reach the poverty and water goals. This region has managed to close only 63 percent of primary education completion rate, 26 percent of gender equality, 84 percent of child mortality, and 72 of maternal mortality ratio gaps envisaged under the MDGs. The goal with the most progress still needed is access to basic sanitation. Acceleration is needed improving maternal health and access to basic sanitation.

Latin America and the Caribbean has already reached the targets on extreme poverty, primary completion, and access to safe water. The region stagnated on the gender equality target, but is very close to reaching it. The region has achieved more than 80 percent of the progress needed to reduce under-5 mortality by two-thirds. However, Latin America and the Caribbean is still lagging behind regarding maternal mortality, as progress in this MDG has been significantly slower than elsewhere, achieving only 57 percent of the distance to the goal.

Middle East and North Africa has also reached the targets on poverty and access to improved sanitation facilities. The region is making progress towards achieving universal primary education, gender equality, and child mortality. However more effort is needed to ensure access to safe drinking water.

South Asia has reached the target on access to safe water and has already achieved to close 85 percent of the gender disparity gap in primary and secondary education goal. There has also been progress on primary completion and child

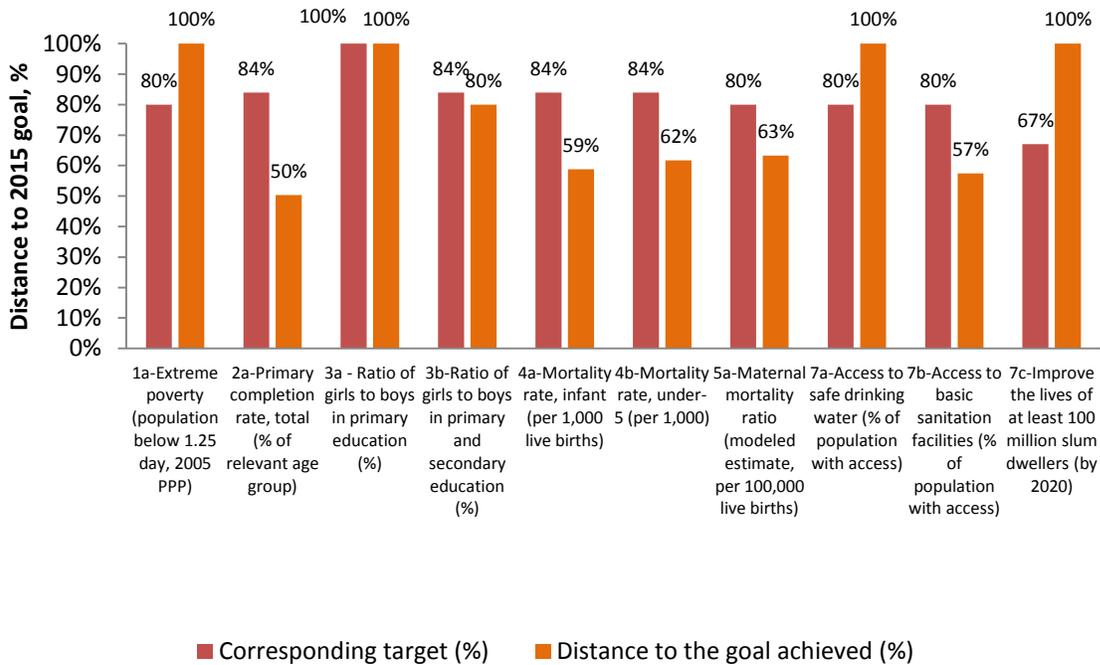
mortality rates. However, poverty reduction has been slower as well as access to basic sanitation. Faster progress is required in terms of reducing child and maternal mortality and improving access to sanitation facilities if the region is to reach these goals by 2015.

Sub-Saharan Africa is lagging with respect to other regions and most MDGs. However, this region was also lagging the most at the starting

date. Currently, Sub-Saharan Africa has achieved more than 40 percent of the progress required to reach, by 2015, goals such as poverty reduction, primary completion, gender parity, primary completion, child mortality, and access to safe water.

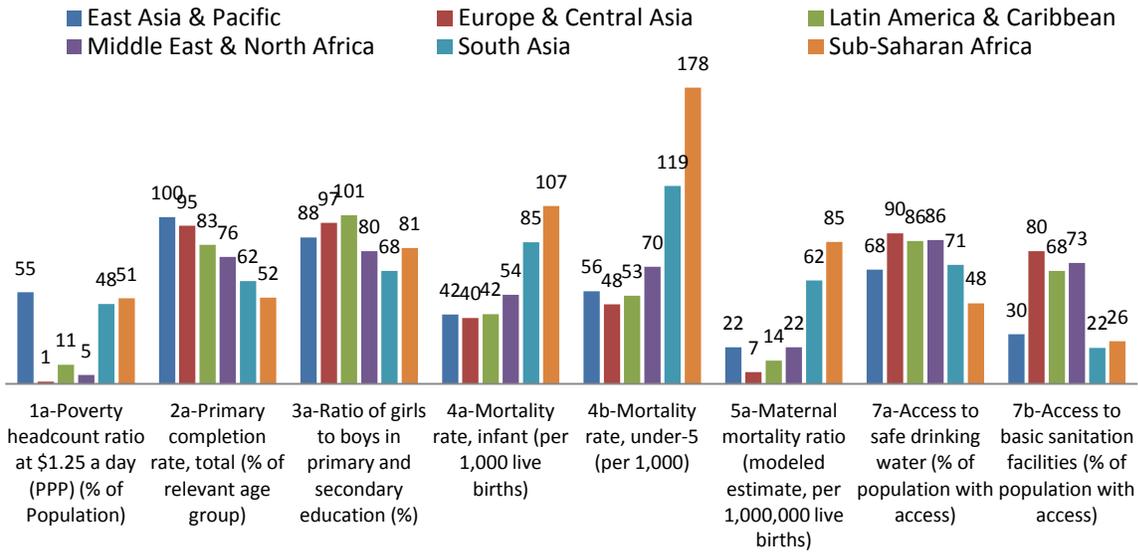
Most countries need to pay particular attention to the health-related MDGs if they are to reach these goals by 2015.

**Figure 1: Global progress toward achievement of the MDGs**  
Developing countries, percent of total required progress between 1990 and 2015, as achieved in 2011 or 2010.



*Note:* Intermediate target calculated using a linear progression over 25 years, resulting in a needed progress of 4 percent per annum. Note that the corresponding target for 2010 would equal 80 percent, and for 2011 84 percent, to be on track to attain the MDG by 2015. Any value above those intermediate targets indicates that the world is ahead of the required pace to meet the MDG. A value of 100 percent means that the MDG has been met.  
*Source:* World Bank staff estimates.

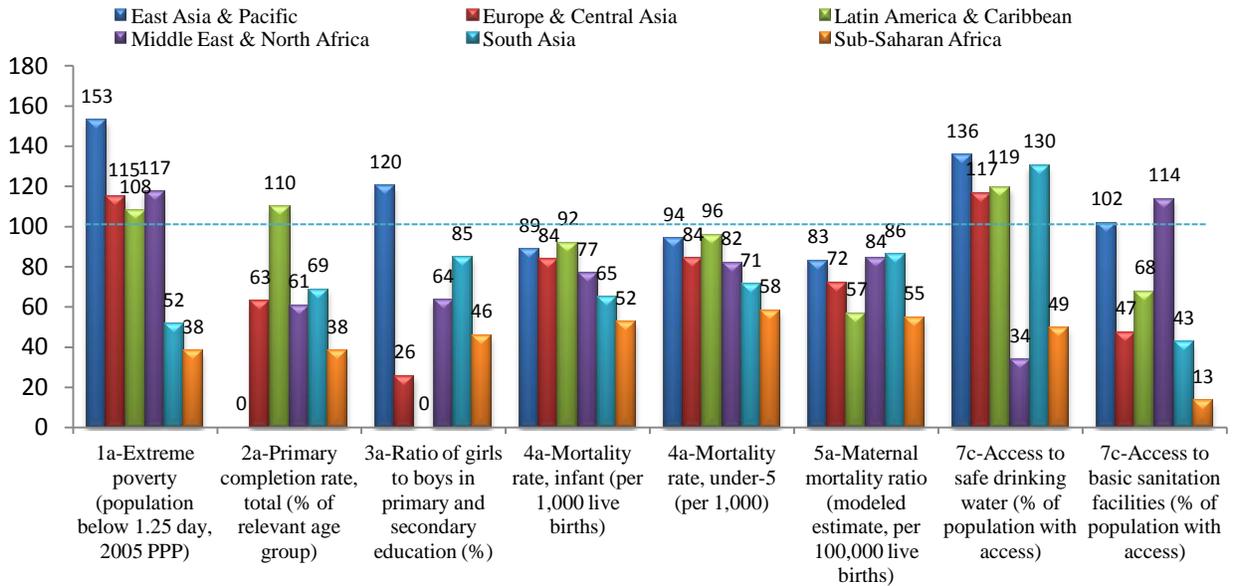
**Figure 2: Starting position on each MDG by region in 1990**



Source: WDI and GMR

**Figure 3: Achieved global progress toward the MDGs**

for 2010, except MDG1a (2008), MDG 4a & b (2011)



Note: Note that corresponding target for 2008 would equal 72 percent, for 2010, 80 percent, and 2011 84 percent. Any value above those corresponding targets indicates that the region seems on track to meeting the MDG using a simple linear approximation. A value larger than 100 percent means that more progress has been made than is necessary at the year reported. A negative value indicates deterioration.

Source: WDI and GMR.

# MDG 1

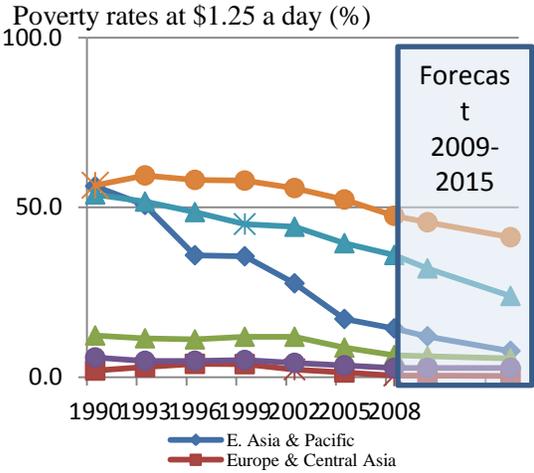
## Eradicating extreme poverty and hunger

The proportion of people living on less than US\$1.25 a day fell from 43.1 percent in 1990 to 22.2 percent in 2008, leaving 1.3 billion people in extreme poverty. Although the food, fuel, and financial crises over the past five years have worsened the situation of vulnerable populations and slowed poverty reduction in some countries, global poverty rates have continued to fall. Between 2005 and 2008, both the poverty rate and the number of people living in extreme poverty fell in all six developing country regions, the first time this has happened. Preliminary estimates for 2010 show that the extreme poverty rate fell further, reaching the global Millennium Development Goal (MDG) target of halving world poverty five years early, lifting 100 million more people out of extreme poverty.

Further progress is possible and likely before the MDGs’ 2015 target date. According to the current growth forecasts, the proportion of people living in extreme poverty will fall from 22.4 percent in 2008 to 15.4 percent by 2015, leaving slightly less than 1 billion people in extreme poverty. Of these, 40 percent will live in South Asia and 40 percent in Sub-Saharan Africa.

The pace of poverty reduction depends not just on the growth of GDP but also on its distribution. A common assumption is that growth will be “distribution neutral”; that is, growth in average income will result in similar changes in the incomes of everyone, rich or poor. This has been the general experience over the past 20 years, but there are notable variations: income distribution has improved in some countries, such as Brazil, while worsening in others, such as China. To accelerate progress toward the elimination of extreme poverty, development strategies should attempt to increase not just the mean rate of growth but also the share of income going to the poorest segment of the population. Sub-Saharan Africa, where average incomes are low and the average incomes of those below the poverty line are even lower, will face great difficulties in bringing its poorest people to an adequate standard of living.

**Figure 1: Poverty rates by region**



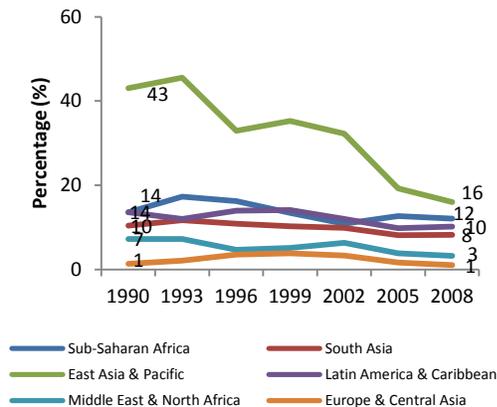
Source: World Bank Povcalnet  
 Note: Regional poverty rates are measured at US\$1.25 a day, with forecasts to 2015 (to be updated).  
 \* Surveys cover less than half of the population

Latin America and the Caribbean, where average incomes are higher, must also overcome extremely inequitable income distributions.

The distribution of the poor is notable in the differences between poverty rates in rural and urban areas (Figure 2). Although global poverty has declined over time, there has not been much of an improvement in the differences between the urban and rural populations below the poverty line. The East Asia and Pacific region was the only region to reduce the gap by more than half by 2008. In other regions, such as Sub-Saharan Africa, Latin America and the Caribbean, and South Asia, the reduction in the difference between urban and rural poverty has been lower.



**Figure 2: The percentage gap in urban-rural poverty headcount has decreased in most regions**



Source: World Development Indicators database, 2013. World Bank Staff calculations.

in undernourishment have stalled, leaving 13 percent of the world’s population, almost 900 million people, without adequate daily food intake.

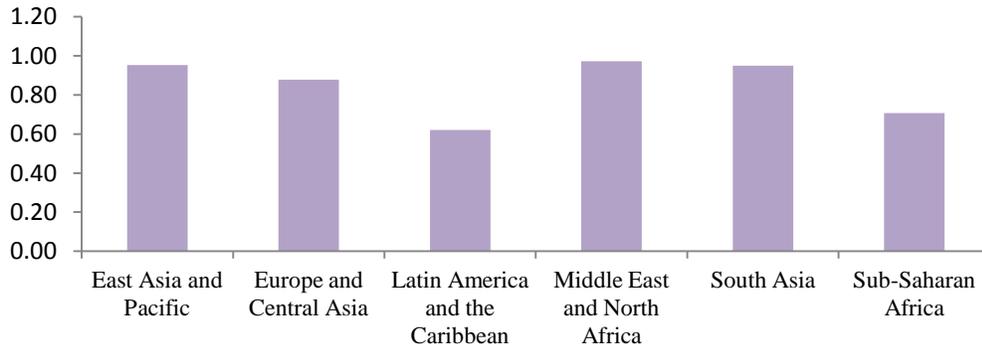
Hunger and malnutrition are measured by two different MDG indicators. Undernourishment reflects a shortage of food energy to sustain normal daily activities, and is affected both by changes in the average amount of food available and by its distribution. After steady declines in most regions from 1991 to 2005, further improvements

Malnutrition, measured in children by comparing their weight with other children of similar age, reflects a shortfall in food energy, poor feeding practices by mothers, and a lack of essential nutrients in their diets. Malnutrition in children often begins at birth, when poorly nourished mothers give birth to underweight babies. Malnourished children develop more slowly, enter school later, and perform less well. Based on available data, malnutrition rates in developing countries have dropped substantially, from 28 percent of children under age 5 in 1990 to 17 percent in 2011. Every developing region except Sub-Saharan Africa is on track to cut child malnutrition rates in half by 2015. However, data collection on malnutrition using

surveys that directly measure children’s weight and height is costly, and many countries lack sufficient information to calculate time trends.

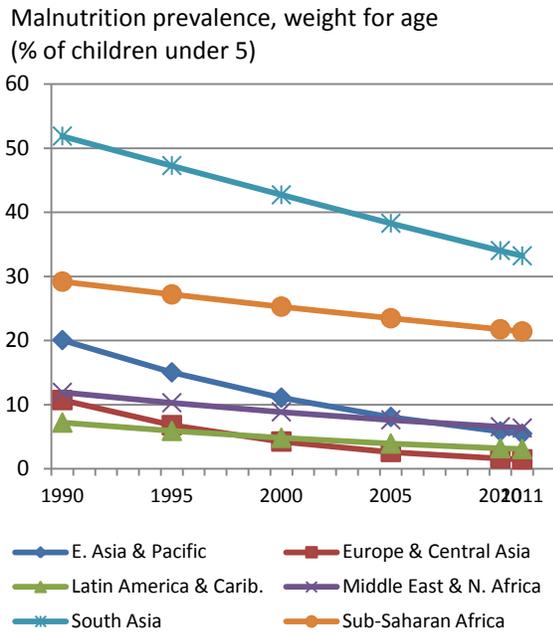
**Figure 3: Average daily income of the poor, 2008**

Average daily income of the poor, 2008  
measured at US\$1.25 a day poverty line (\$)



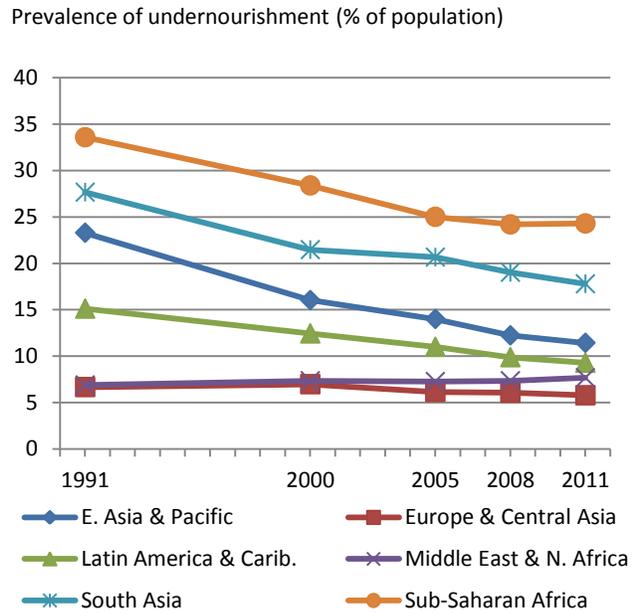
Source: World Bank, Povcalnet.

**Figure 4: Malnutrition prevalence by region, 1990-2011**



Source: World Development Indicators database 2013.

**Figure 5: Undernourishment prevalence by region, 1991-2011**



# MDG 2

## Achieve universal primary education

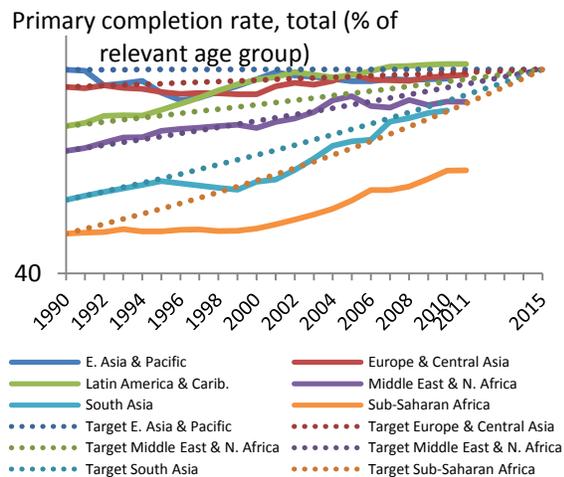
The commitment to provide primary education to every child is the oldest of the MDGs, having been set at the first *Education for All* conference in Jomtien, Thailand, more than 20 years ago. Achieving this goal has often seemed tantalizingly near, but it has been reached only in Latin America and the Caribbean, although East Asia and Pacific and Europe and Central Asia are close. Progress among the poorest countries, slow in the 1990s, has accelerated since 2000, particularly in South Asia and Sub-Saharan Africa, but full enrollment remains elusive. Many children start school but drop out before completing the primary stage, discouraged by cost, distance, physical danger, and failure to progress. Even as countries approach the MDG target, the education demands of modern economies are expanding. In the 21<sup>st</sup> century, primary education will be of value only as a stepping stone toward secondary and higher education.

In most developing regions, school enrollment rates picked up after the MDGs were promulgated in 2000, when the completion rate was 80 percent. By 2009, nearly 90 percent of children in developing countries completed primary school, but completion rates have stalled since. East Asia and the Pacific, Europe and Central Asia, and Latin America and the Caribbean have attained or are the verge of attaining complete primary education. Completion rates in the Middle East and North Africa have stayed at 90 percent since 2008. Sub-Saharan Africa and South Asia, which started out farthest behind, have made substantial progress in absolute terms: South Asia has reached 88 percent but progress has been slow, while Sub-Saharan Africa lags far behind, at 70 percent. Even if schools in these regions were to begin now to enroll every eligible child in the first grade, those children would not be able to achieve a full course of primary education by 2015. But it would help.

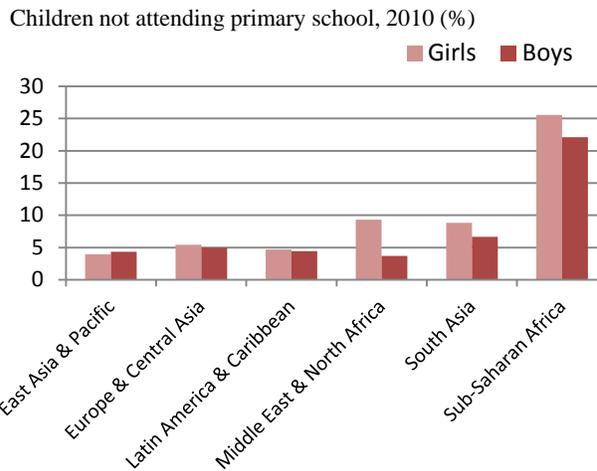


Many children enroll in primary school but attend intermittently or drop out entirely. This is particularly true for girls, whose work is needed at home. Almost all school systems with low enrollment rates show under-enrollment of girls in primary school. In rural areas, the work of children of both sexes may be needed during planting and harvest. Other obstacles, including the lack of suitable facilities, absence of teachers, and school fees, discourage parents from sending their children to school. The problem is worst in South Asia and Sub-Saharan Africa, where more than 48 million children of primary school age are not in school.

**Figure 6: Progress toward achieving complete primary education is leveling off**



**Figure 7: More girls than boys remain out of school**

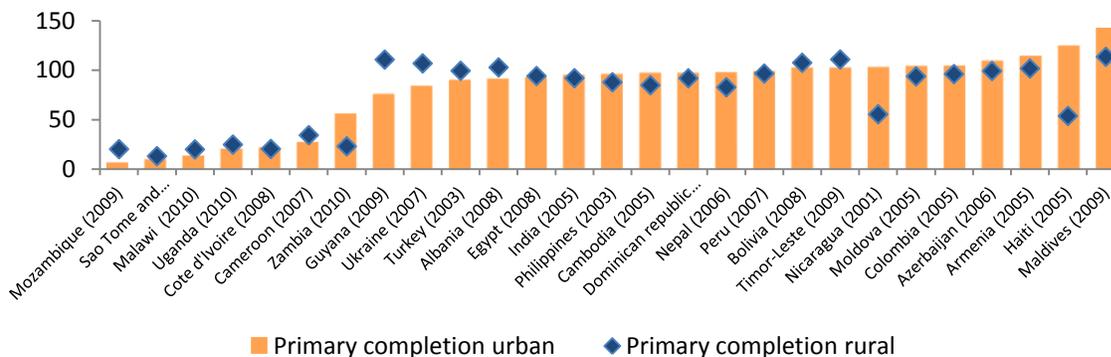


Note: Progress assessment in East Asia and Pacific does not include China, which is believed to have close to 100 percent completion rates.

Source: UNESCO Institute of Statistics and World Development Indicators database.

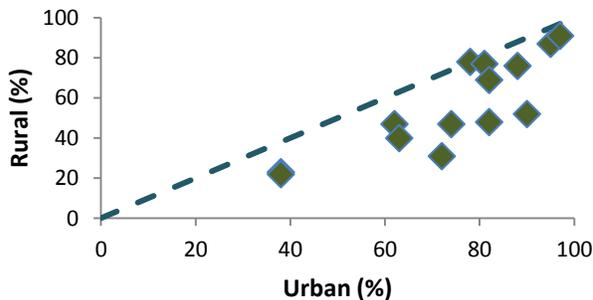
Urban and rural primary completion rates are very similar in many countries around the world (Figure 8). The *quality* of primary education, however, differs more substantially, as evidenced by the notable differences in the percentage of pupils reaching competency levels in reading in urban versus rural areas (Figure 9).

**Figure 8: Worldwide urban and rural primary completion rates are not very different**



Source: World Bank 2012 and staff calculations.

**Figure 9: Percentage of pupils reaching reading competency level (4-8) in urban and rural areas (2007)**



*Source:* Southern and Eastern Africa Consortium for Monitoring Educational Quality (SACMEQ).

In Ghana, enrollment in basic education has nearly doubled in the past 15 years, to 7 million pupils in 2011, and government expenditure on basic education in the past decade has more than tripled in real terms. More children are accessing basic education, graduating from junior high school, and enrolling in senior high school than at any time in Ghana's history.

Despite Ghana's achievements in access to basic education, inequity remains a persistent feature of its education service delivery and its most critical challenge. Primary net enrollment ratio (NER) has remained close to 80 percent over the past five years, meaning that nearly 1 million primary school-aged children are not in school. These students are disproportionately from poor households and rural or marginalized areas or language groups (including the three northern regions) or are living in situations of fosterage. Instead of compensating for deprivation, public expenditures appear to exacerbate the inequality by allocating fewer resources per child to the regions with the majority of deprived districts.

Such a system perpetuates poverty and inequality. This picture of inequity is mirrored in data on Ghanaian children's primary learning outcomes, primary completion rates, and access to senior high school. Notably, while several equity-improving initiatives have been introduced by the Ministry of Education, challenges in program design, targeting, and implementation have resulted in these initiatives disproportionately benefitting individuals from wealthier populations. Hence, Ghana's scores in the Trends in International Math and Science Study (TIMSS) 2003 were lower than all of the other countries evaluated, such as South Africa, Botswana, Morocco, Tunisia, and Egypt. In TIMSS 2007, Ghana's scores were also among the lowest, behind Algeria, Botswana, Egypt, and Tunisia.

Efficiency improvements in the use of money, human and physical resources, and time could help Ghana realize improved learning outcomes within the same budget envelope. The education sector accounts for over 20 percent of government expenditures, equivalent to 6 percent of GDP. Over the past decade, education expenditures have surpassed enrollment growth by a ratio of 3 to 2. Efficiency improvements in the deployment and utilization of teachers (e.g., more equitable distribution and reduced absenteeism) and improved time on task (i.e., the amount of time used for learning during the school day) could help the Ministry of Education and the Ghana Education Service improve learning outcomes at no additional cost.

# MDG 3

## Promote gender equity and empower women

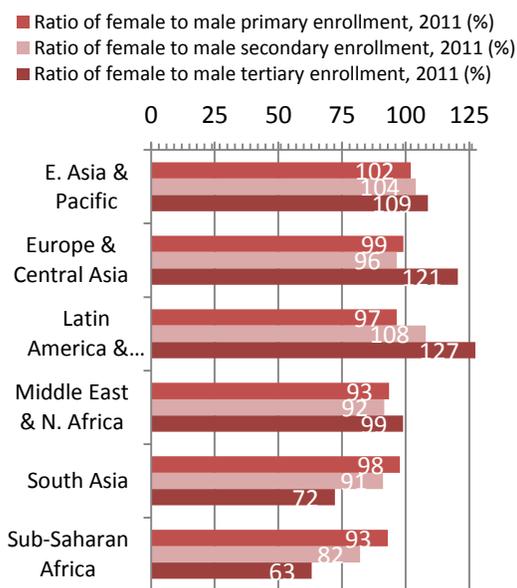
Women make important contributions to economic and social development. Expanding opportunities for them in the public and private sectors is a core development strategy. Education is the starting point. By enrolling and staying in school, girls gain the skills they will need to enter the labor market, care for families, and make decisions for themselves. Achieving gender equity in education is an important demonstration that young women are full, contributing members of society.



Girls have made substantial gains in primary and secondary school enrollment. In 1990, the primary school enrollment rate of girls in developing countries was only 86 percent that of boys. By 2011, the average was 97 percent.<sup>7</sup> Similar improvements have been made in secondary schooling, where girls' enrollments have risen from 78 percent to 96 percent of that of boys. In many countries, girls' secondary school enrollments have surpassed those of boys. Progress has been greatest in richer countries. In countries classified by the World Bank as upper-middle-income, girls' enrollments in primary and secondary schools now exceed those of boys. But averages can

obscure large differences between countries: over-enrollment of girls in one country does not counterbalance under-enrollment in another. At the end of the 2011 school year, 31 upper-middle-income countries had reached or

**Figure 10: Gender parity in primary, secondary, and tertiary education**



<sup>7</sup> The ratio between the enrolment rate of girls and boys (gender parity ratio) increased from 91 in 1999 to 97 in 2010 for the developing regions as a whole – falling within the plus-or-minus 3-point margin of 100 percent that is the accepted measure for parity.

Source: UNESCO Institute of Statistics and World Development Indicators database.

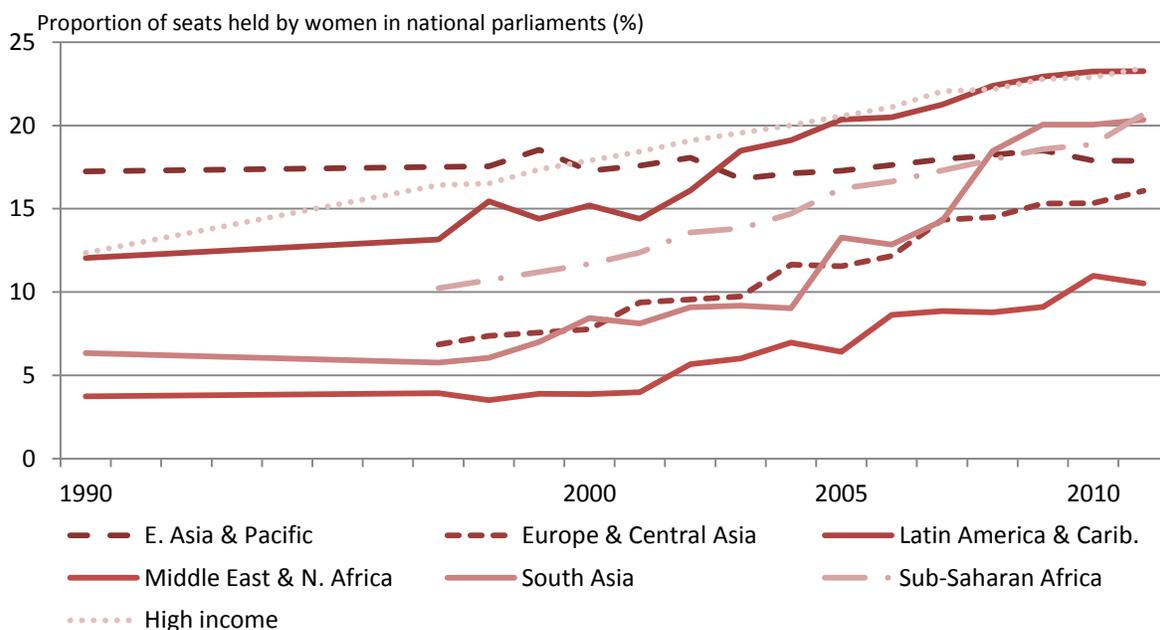
exceeded equal enrollment of girls in primary and secondary education; 23 lower-middle-

income countries had reached this threshold; but only nine low-income countries had done so. Two regions lag behind: South Asia and Sub-Saharan Africa.

More women are participating in public life at the highest levels. The proportion of parliamentary seats held by women continues to increase. Latin America and the Caribbean, where women now hold 23 percent of all

parliamentary seats, remains in the lead. The most impressive gains have been made in South Asia, where the number of seats held by women more than tripled between 1999 and 2010. In Nepal, women held one-third of parliamentary seats in 2011. In Sub-Saharan Africa, Rwanda leads the way: since 2008, 56 percent of its parliamentary seats have been held women. The Middle East and North Africa lags far behind.

**Figure 11: Women in parliament**



Source: Interparliamentary Union and World Development Indicators database.

Full economic empowerment of women remains a distant goal. While many women work long hours and make important contributions to their families' welfare, they often work in the informal sector, typically as unpaid family workers. Women's share in paid employment in the non-agricultural sector has risen marginally but remains less than 20 percent in the South Asia and in the Middle East and North Africa. The largest proportion of working women is found in Europe and Central Asia, where in recent years, 47-48 percent of non-agricultural wage employees were women.

# MDG 4

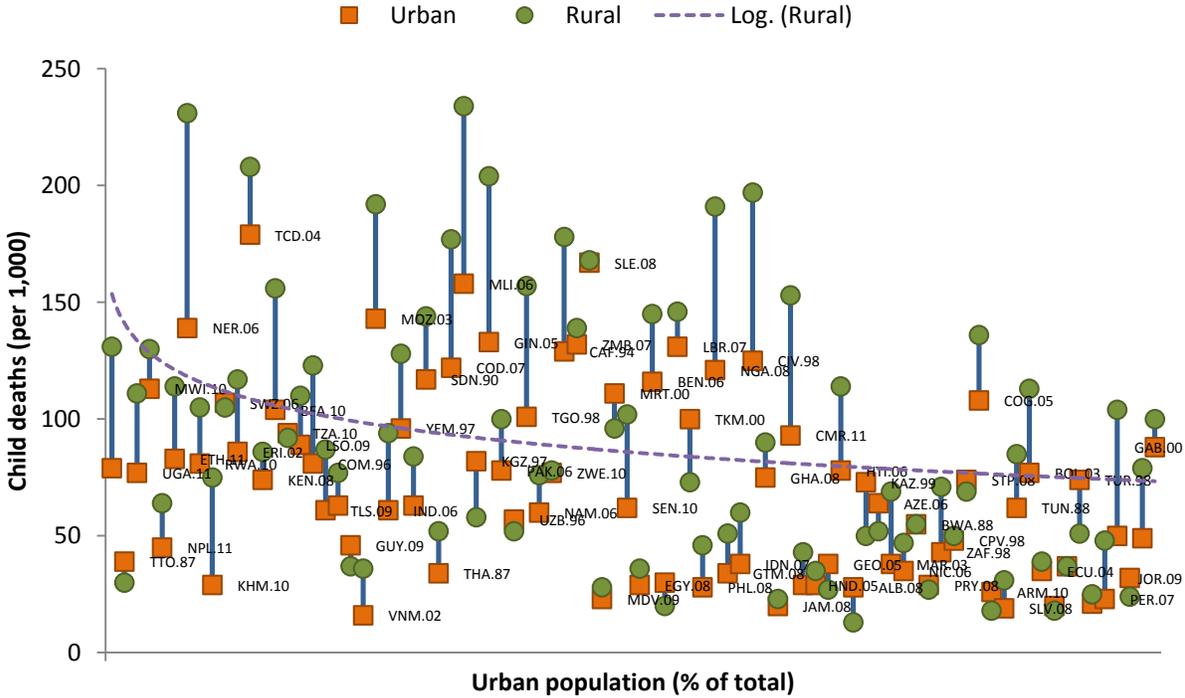
## Reduce child mortality

In most countries around the world, most children’s deaths occur in the first year. The MDG health indicators have seen the least progress of all the MDGs. In developing countries, the mortality rate fell from 87 per 1,000 in 1990 to 51 in 2011. This progress is not sufficient to meet the health-related MDG target of a two-thirds reduction by 2015. Only 25 countries have achieved this target and 26 more have made sufficient progress to meet the target by 2015.

For the infant mortality rate, the numbers are even worse: only 5 countries met the target and only 13 countries are making enough progress to reach it by 2015. There are still more than 120 countries with insufficient progress or that will not meet the goal on time.

In the context of this report, it is important to note that as countries become more urbanized, the difference between the mortality rates of rural and urban children reduces. Notably, the highest rates of child mortality are in Sub-Saharan Africa, whose countries are the least urbanized.

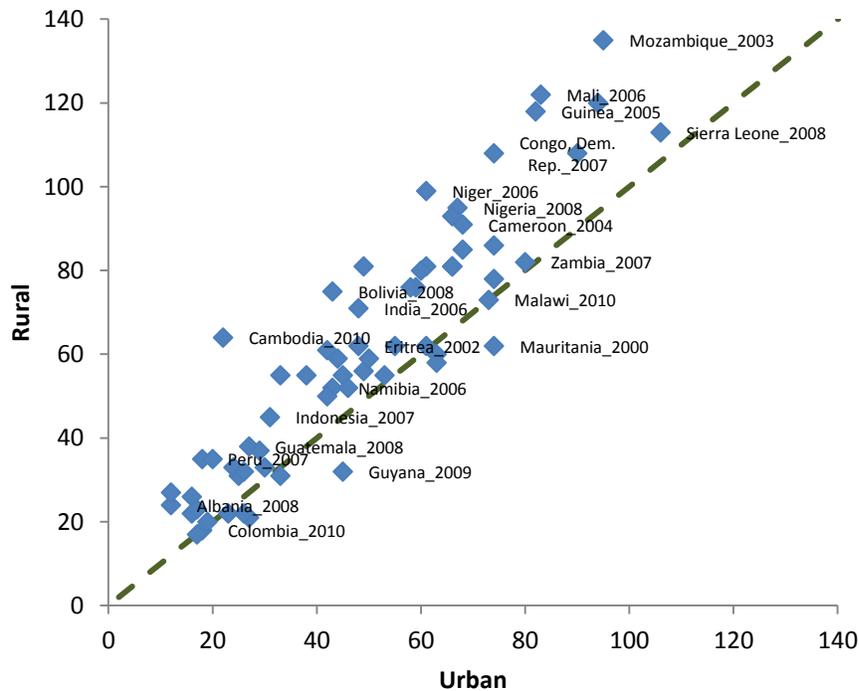
**Figure 12: As countries become urbanized, the child mortality gap between urban and rural areas is reduced, as is the number of children that die before the age of 5.**



Source: Demographic and Health Surveys (DHS).



**Figure 13: Infant mortality is higher in rural areas than in urban ones**



A similar picture emerges with respect to infant mortality, as the disparities between urban and rural infant mortality rates are high worldwide. Higher infant mortality rates in rural areas are in part attributable to the disadvantages faced by rural households, such as lack of access to a safe source of drinking water and electricity. As discussed in Chapter 2, governments need to provide basic services in rural areas as well as urban ones to correct such deficiencies (O'Donnell *et al.* 2009).

Source: Demographic and Health Surveys (DHS), and World Bank staff calculations.

# MDG 5

## Reduce maternal mortality

MDG 5 centers on improving maternal health, with a target of reducing the maternal mortality ratio by three-quarters between 1990 and 2015. With only two years remaining before the target date, progress on maternal health is still lagging. Even though some developing countries have made progress towards reducing maternal mortality (for example, Sri Lanka and Malaysia), progress remains slow for most, and the level of maternal mortality remains high in much of the developing world. Although on the aggregate the rate of progress has doubled across the globe from 2005 to 2010, it is unlikely that this MDG will be achieved by 2015.

South Asia is the only region on track to reduce maternal mortality, assuming it continues at the same rate of progress made from 2005 to 2010 (Figure 14). The Middle East and North Africa might also be able to reach the MDG target if the region doubles the effort it made from 2005 to 2010. The starting point in the level of

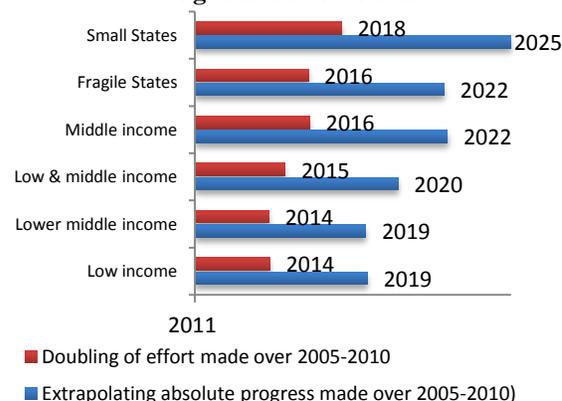
maternal mortality obviously affects progress made in achieving the target, but is not the only factor. Europe and Central Asia started with 70 maternal deaths per 100,000 live births in 1990, while Sub-Saharan Africa started with 850. However, if Sub-Saharan Africa doubles the effort made during 2005 to 2010, it will be able to reach its goal by 2016, while Europe and Central Asia would need to more than double its effort to meet the goal on time.

The starting point for the maternal mortality ratio in middle-income countries in 1990 was nearly half that of low-income countries (370 deaths per 100,000 live births compared to 810). However, middle-income countries as a group are not close to achieving the goal on time either (Figure 15). Only by doubling their effort will they be able to reduce maternal mortality by 2016.

**Figure 14: Year when the maternal mortality goal is expected to be met by region**



**Figure 15: Year when the maternal mortality goal can be expected to be met by income level and by fragile and small states**



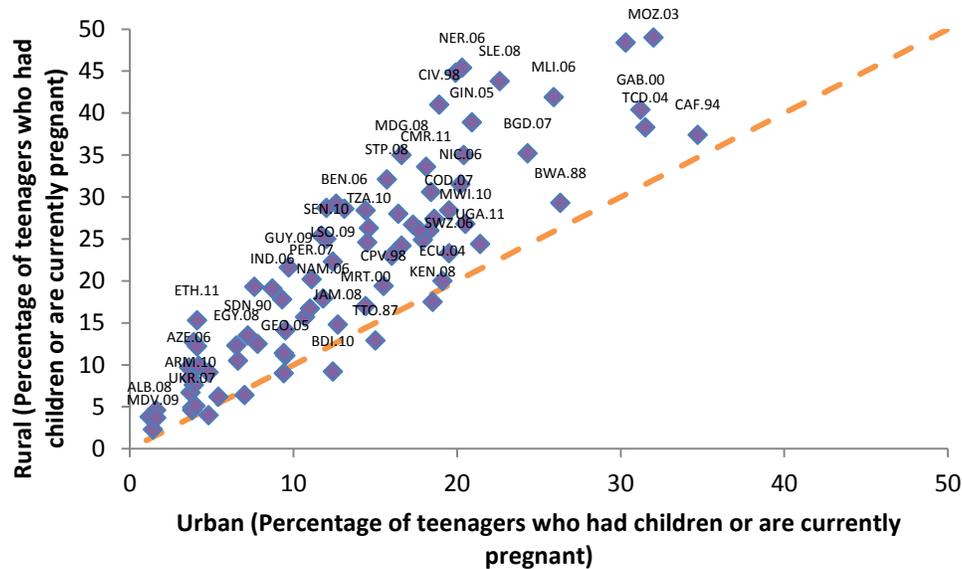
Source: World Development Indicators database 2013.



Despite this bad news, there are some bright spots. Even some countries classified as fragile states have managed to achieve this particular MDG. Fragile states as a group started with a similar number of maternal deaths to Sub-Saharan Africa (780 deaths per 100,000 live births in 1990). Nepal, which is considered a fragile state, reduced its maternal mortality rate from 770 deaths per 100,000 live births in 1990 to 170 in 2010, earning it the MDG Millennium Award in 2010. Nepal has also made extraordinary progress in reducing its proportion of poor people in recent years. Other fragile states such as Afghanistan, Angola, Eritrea, Syria, Timor-Leste, and Yemen are still on track to meet the MDG, some with acceleration, and others following their current growth trend.

The issue of teenage pregnancy still requires significant attention, especially in rural areas, where the rate of teen pregnancy is higher than in urban areas (Figure16).

**Figure 16: The percentage of teenagers who had children or are currently pregnant is higher in rural areas than in urban ones**



Source: Demographic and Health Surveys (DHS).

# MDG 6

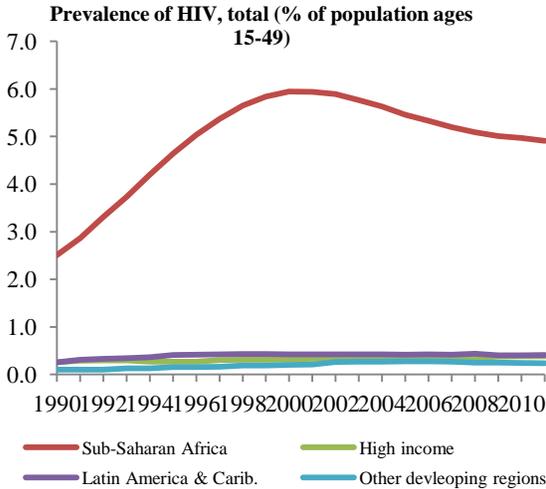
## Combat HIV/AIDS, malaria, and other diseases

Epidemic diseases exact a huge toll in human suffering and lost opportunities for development. Poverty, armed conflict, and natural disasters contribute to the spread of disease and are made worse by it. In Africa, the spread of HIV/AIDS has reversed decades of improvement in life expectancy and left millions of children orphaned. It is draining the supply of teachers and eroding the quality of education. Malaria takes a large toll on young children and weakens adults at great cost to their productivity. Tuberculosis caused the deaths of a million people in 2011, most of them aged 15–45, and sickened millions more. Tuberculosis is one of the principal causes of adult death from a single infectious agent in developing countries.

There were 34 million people living with HIV/AIDS in 2011 and 2.5 million more people had acquired the disease. Sub-Saharan Africa remains the center of the HIV/AIDS epidemic, but the proportion of adults living with AIDS has begun to fall while the survival rate of those with access to antiretroviral drugs has increased. By the end of 2010, 6.5 million people worldwide were receiving antiretroviral drugs. This represented the largest one-year increase in coverage, but fell far short of the target of universal access. In Africa, 58 percent of adults with HIV/AIDS are women; among youth aged 15-24, the prevalence rate among women is more than twice that of men. Latin America and the Caribbean has the second highest prevalence rate, with 0.5 percent of adults infected (Figure 17).

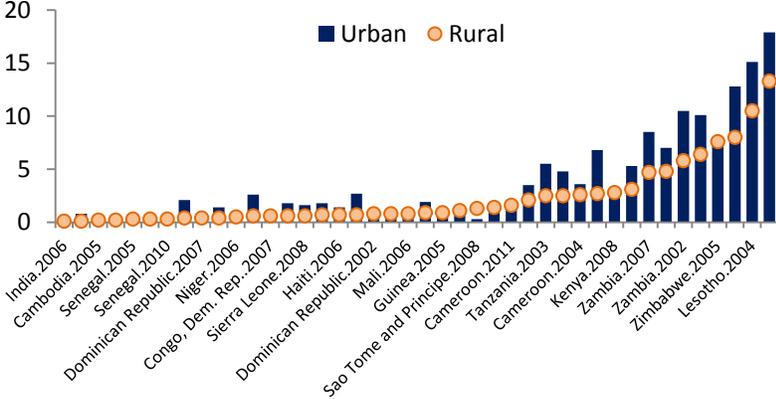
The prevalence of HIV infection in urban and rural areas is shown in Figure 18 for a number of countries. For most Sub-Saharan Africa countries, the rates of HIV infection are higher in urban areas than in rural ones. Since evidence from health surveys confirms that a prominent

**Figure 17: Percent of population aged 15-49 with HIV**



Source: UNAIDS and World Development Indicators database.

**Figure 18: HIV prevalence among population aged 15-24 years**



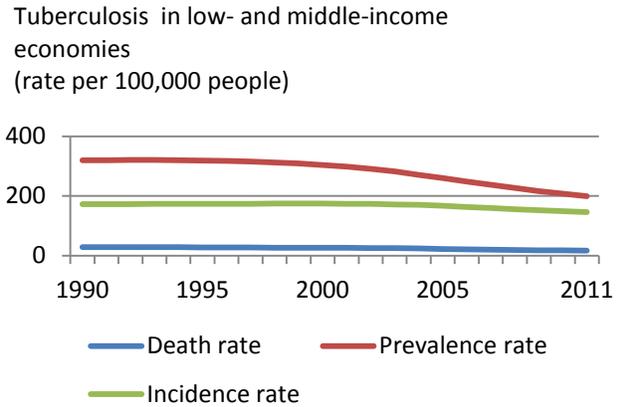
Source: Demographic and Health Surveys (DHS).

decline in prevalence is associated with higher education, increased condom use, and a reduced

number of sexual partners, most of the effort to prevent HIV/AIDS should still be concentrated in urban areas.

In 2011, there were 8.7 million people newly diagnosed with tuberculosis, but its incidence, prevalence, and death rates are all falling (Figure 19). The global incidence rate peaked in 2002; the prevalence rate – the proportion of people living with tuberculosis – began to fall in 1997. If these trends are sustained, the world could achieve the target of halting and reversing the spread of this disease by 2015. People living with HIV/AIDS, which reduces resistance to tuberculosis, are particularly vulnerable, as are refugees, displaced persons, and prisoners living in close quarters and unsanitary conditions. Well-managed medical intervention using appropriate drug therapy is the key to stopping the spread of tuberculosis.

**Figure 19: Number per 100,000 infected with tuberculosis in low-and middle-income countries**



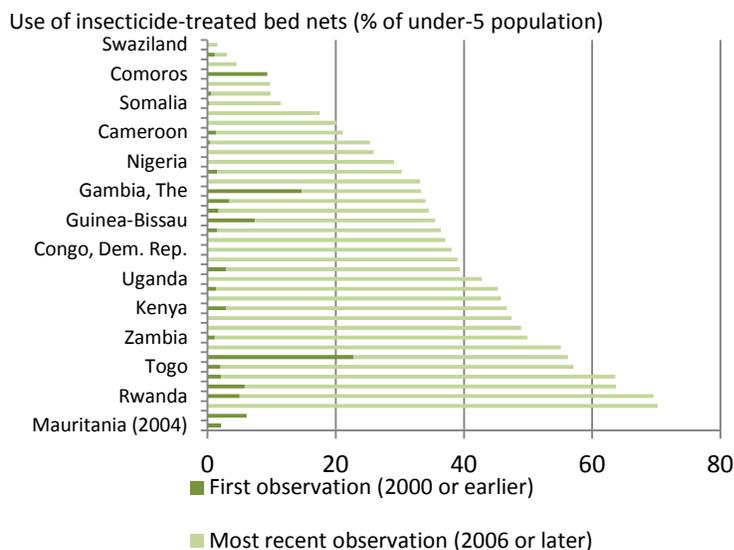
Source: UNICEF and World Development Indicators database.



There are 300–500 million cases of malaria each year, leading to more than 1 million deaths.

Malaria is a disease of poverty, but there has been recent progress against the disease. In

**Figure 20: Percent of under-5 population using insecticide-treated bed nets**



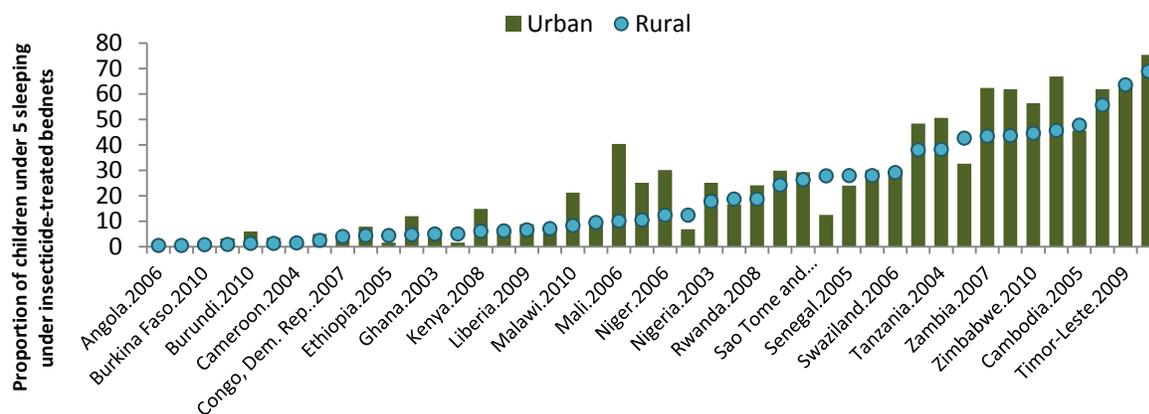
Source: UNICEF and World Development Indicators database.

2011, Armenia was added to the list of countries certified free of the disease. Although malaria occurs in all regions, Sub-Saharan Africa is the

epicenter of the disease, where the most lethal form of the malaria parasite is most abundant. Prevention and control measures, such as the use of insecticide-treated mosquito nets, have proven effective and their use is spreading. The use of nets in Sub-Saharan Africa is estimated to have grown from 2 percent in 2000 to 39 percent in 2010. Better testing and the use of combination therapies with artemisinin-based drugs are improving the treatment of at-risk populations. But malaria is a difficult disease to control.

There is evidence of emerging resistance to artemisinins and to pyrethroid insecticides used to treat mosquito nets.

**Figure 21: Proportion of children under age 5 sleeping under insecticide-treated bed nets in urban versus rural areas**



Source: Demographic and Health Surveys (DHS).

There are minor differences in the rate of use of insecticide-treated mosquito nets between rural and urban areas (Figure 21). The cost of distributing nets is lower in urban areas due to agglomeration effects, likely contributing to the higher usage there.

# MDG 7

## Ensure environmental sustainability

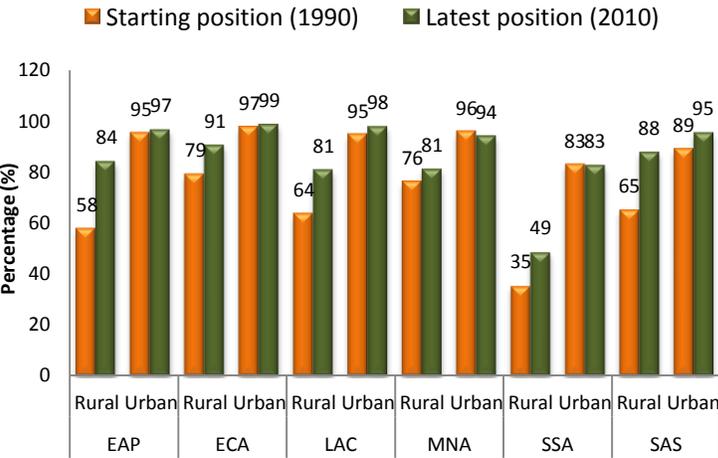
As part of the MDGs, most countries have agreed on the principles of sustainable development and there is international consensus to protect the environment. Considering this, MDG 7 includes a target of halving the proportion of the



population without access to improved sanitation and water sources by 2015. However, access to safe water and sanitation remains a problem for people of most developing countries.

There are still 56 countries that have not made enough progress to reach on time the MDG target to halve the proportion of the population without access to improved water sources; moreover, 20 countries do not have enough data to determine whether or not they will reach the target by 2015. Sub-Saharan Africa is lagging the most, although it has improved access in rural areas from 35 percent in 1990 to 49 percent in 2010; access in urban areas has not changed and remains at 83 percent. East Asia and Pacific managed to make impressive improvements in rural areas, from a starting position of only 58 percent in 1990 to 84 percent in 2010, and in urban areas reaching nearly 100 percent by 2010 (Figure 22). In general, the other regions have already managed to reach access rates of more than 80 percent in urban and rural areas.

**Figure 22: Access to water by region -- starting and most recent data available (2010)**



Source: World Development Indicators database 2013.

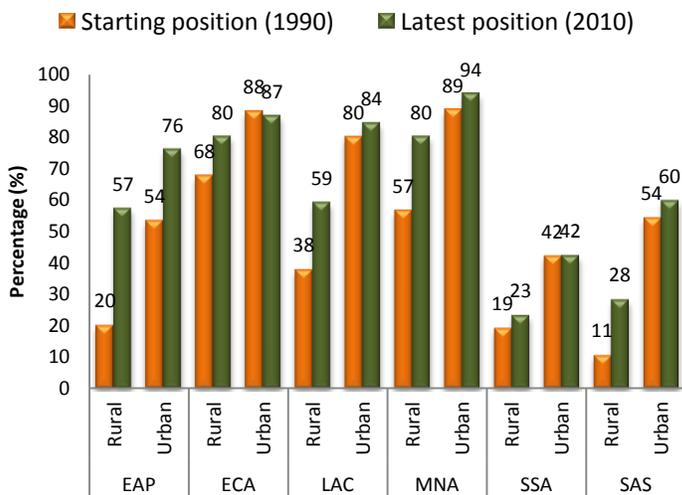
Poor sanitation causes millions of people worldwide to contract illnesses. Around 1.7 million people die each year because of unsafe water and sanitation, and 90 percent of those are children under the age of five. However, almost all sanitation-related deaths occur in the rural areas of developing countries, where sanitation problems are more severe (and there is less access to adequate health care). Some regions have made more progress than others, but it is important to look at the differences in access to improved sanitation by urban and rural areas.

As expected, sanitation in rural areas remains worse than in urban areas despite the fact that most regions have improved their access to sanitation in rural areas by more than 20 percentage points. South Asia and Sub-Saharan Africa are the only regions where progress has not been significant, with an increase of only 17 percentage points in South Asia and 4 percentage points in Sub-Saharan Africa from 1990 to 2010. In addition to the less than stellar

improvements, these regions also had the worst starting positions.

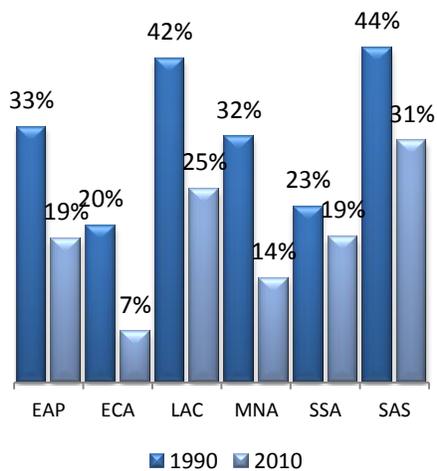
In urban areas, the increase in access to improved sanitation has not been impressive either, with the biggest advance also made in the East Asia and Pacific region, where there was an increase of around 22 percent during the same period (Figure 23).

**Figure 23: Access to sanitation by region -- starting and most recent data available (2010)**



Source: World Development Indicators database, 2013.

**Figure 24: Urban-rural gap in access to sanitation by region**



Although there is a long way to go with this MDG, the gap between urban and rural access to sanitation in all regions has decreased over time (Figure 24). In 1990, the gap was about 42 percent in Latin America and the Caribbean and 44 percent in South Asia; in 2010 this gap was only 25 percent in Latin America and the Caribbean, and 31 percent in South Asia. Most strikingly, in Europe and Central Asia, this gap decreased from 20 percent in 1990 to 7 percent in 2010. This indicates that even though progress is slow, the underserved populations in the rural areas are catching up.

# MDG 8

## Develop a global partnership for development

The use of information and communications technology (ICT) for economic development is part of the MDG 8 indicator, which focuses on the deepening of a global partnership for development. A specific description of this sub-MDG was chosen and indicators identified. Target 8F states that in cooperation with the private sector, the benefits of new technologies, especially those related to information and communications, will be made available. The indicators to be monitored to this effect are the number of fixed telephone lines, cellular subscribers, and internet users (Figure 26).

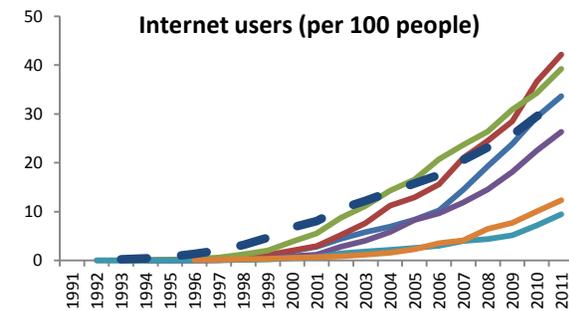
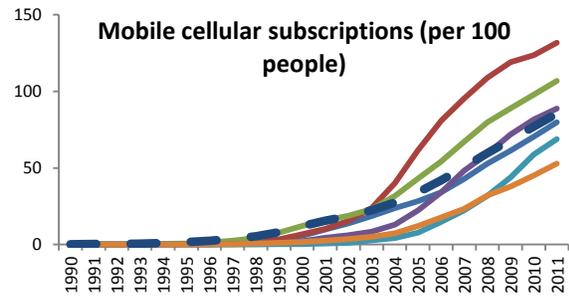
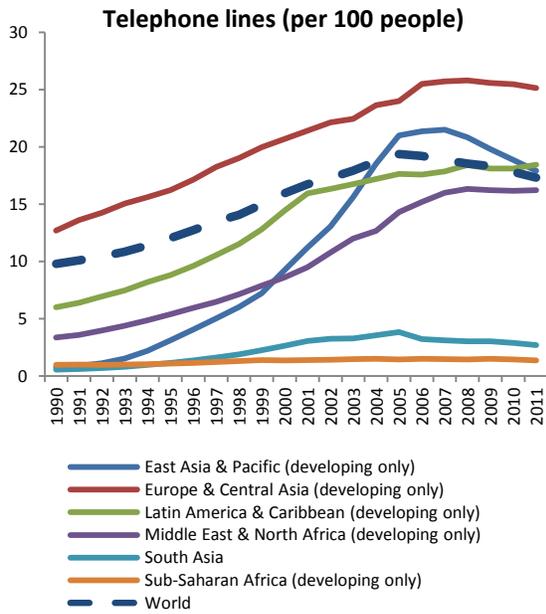
These indicators show that mobile phone subscriptions have risen impressively across the

world, while the growth in the number of fixed telephone lines has stagnated. Remarkable increases have also taken place in internet usage, although here progress is more diverse, with stronger growth in high-income countries than in low- and middle-income countries. Even though access challenges remain, particularly in low-income countries, the spectacular rise in mobile phone penetration has allowed for a variety of innovations to emerge that allow citizens, governments, and international organizations to be more engaged and better informed, and that enable aid programs to identify and communicate more directly with beneficiaries.

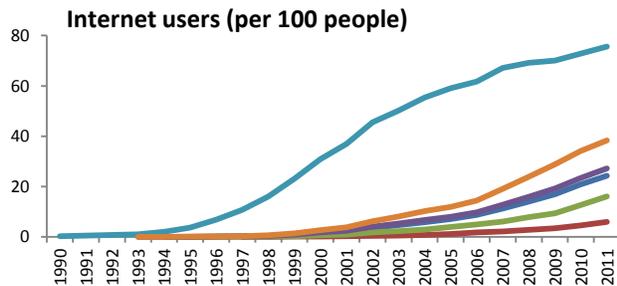
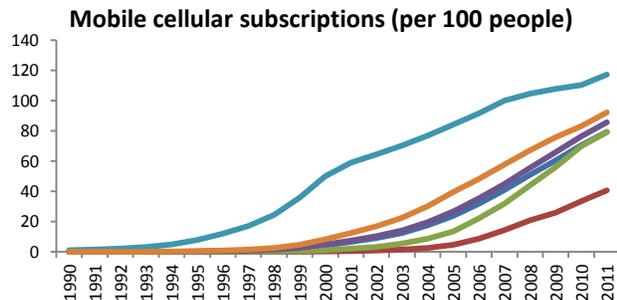
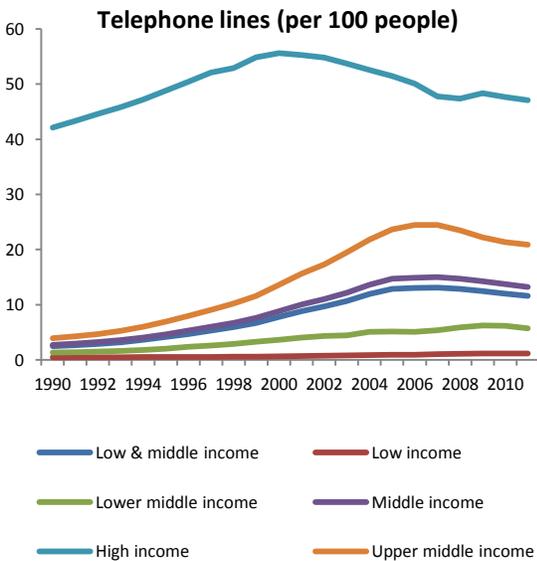


**Figure 25: Prevalence of ICT usage by region and income group**

**By region:**



**By income group:**



**Reference**

O'Donnell, Owen, Ellen Van de Poel, and Eddy Van Doorslaer. 2009. "What Explains the Rural-Urban Gap in Infant Mortality: Household or Community Characteristics?" *Demography* Vol. 46 (4): 827-850.

## Improving the measurement of development goals

The Millennium Development Goals provide a yardstick against which to measure development outcomes. They have also stimulated demand for better statistics and new programs to increase the capacity of developing countries to produce and use statistics. The United Nations and its specialized agencies, including the World Bank and the IMF, and the OECD responded to these demands by creating new partnerships and mobilizing additional resources to provide support for statistics in developing countries. The result has been a marked improvement in the quality and availability of statistics on core development outcomes: poverty and income distribution, school enrollments, mortality and morbidity rates, and environmental conditions.

The MDGs posed three challenges: the selection of appropriate targets and indicators with which to monitor them; the construction of an international database to use for global monitoring; and the need for significant improvements in the quality, frequency, and availability of the relevant statistics, especially at the national level. The selection of goals and targets was determined by the Millennium Declaration adopted unanimously by the member states of the United Nations. Building the database and strengthening the statistic systems of developing countries has required the efforts of many partners over many years. When countries produce statistics to monitor their own development programs, there are often differences in definition and methodology that limit comparability across countries. Whether monitored at the national, regional, or global level, international monitoring of the MDGs requires indicators that are comparable across countries and over time.

To produce harmonized statistics suitable for international comparisons, agencies often revise national data or recompile data using different reference periods or standards, such as the “dollar a day” poverty indicator. They may also impute values for missing data or use statistical models to combine multiple estimates. Interagency efforts such as these have been very important for filling the gaps in child and maternal mortality series. However, they inevitably result in data series that differ from nationally reported data and international assessments of country progress that differ from those produced by the countries.

At the time the MDGs were adopted, few developing countries had the capacity or resources to produce statistics of the requisite quality or frequency. Many countries had not conducted a recent census or a household survey capable of producing information on income, consumption, or health status. Values for many indicators disseminated by international agencies were based on unverified reports from national authorities. Statistical activities sponsored by bilateral donors and multilateral agencies often focused narrowly on securing data of interest to them but doing little to increase the capacity of the national statistical system to serve the needs of local decision makers or citizens.

The early efforts to monitor the MDGs revealed large gaps in both the international database and in many national databases. In 2003-2004, the Partnership in Statistics for Development in the 21st Century (PARIS21) conducted six case studies of developing country statistical systems. The general finding of the studies was one of very limited capacity to manage their own statistical programs:

The systems are characterized by under-funding, reliance on donor support, particularly for household surveys, and very weak administrative data systems. The basic demographic information needed to

underpin key indicators is out of date in some countries, and funding for major activities, such as population censuses, is particularly difficult to secure. Overall, there is a shortfall in funding for core statistical systems required to provide information both for economic management and for monitoring the MDGs. (PARIS21 2004, page 5).

The proportion of countries with two or more data points (the bare minimum needed for assessing trends) for selected MDG indicators in 2005 and 2013 is shown in Table 1. For some indicators, the improvement has been much more dramatic. In 2005, no country had two or more comparable estimates of maternal mortality ratios; in 2013, there were 132. But for other less prominent indicators, progress has been slower.

**Table 1: Proportion of countries with two or more observations (%)**

	2005 Database (154 developing countries)				2013 Database (143 developing countries)*			
	1990-1994	1995-1999	2000-2004	1990-2003	1990-1994	1995-1999	2000-2004	1990-2011
Poverty	10	25	2	47	17	24	28	65
Malnutrition	14	18	5	56	15	17	17	78
Primary completion	51	67	72	84	48	57	76	90
Gender	0	60	69	82	54	57	80	92
U5 mortality	3	3	3	96	99	99	99	99
Water	0	0	0	66	87	97	97	97
Sanitation	0	0	0	61	83	95	97	97

\*World Bank low- and middle-income economies.

Despite the progress made in the last decade, national systems face immense difficulties on many fronts including funding, sectoral shortcomings and poor data access, and the development of skills needed to use statistics effectively in planning and management. In 2009, the High Level Forum on Development Effectiveness in Busan endorsed a new action plan for statistics. Several statistical domains have been identified as priorities for international action because of large deficits of data quality and availability. The high priority domains include: agricultural statistics, poverty statistics and household surveys, gender statistics, labor force statistics, environmental accounting and the system of national accounts, and vital registration systems. The Busan Action Plan for Statistics provides an agreed framework for addressing capacity limitations in developing countries and work is already underway in some domains. However, resources are limited and even with greater resources, capacity building is a slow, deliberate process. The MDGs have contributed to the development of a statistical infrastructure that is increasingly capable of producing reliable statistics on a variety of topics.

## Reference:

PARIS21. 2004. *Report on Six Case Studies*.

# 1. Macroeconomic, Trade, Aid Developments, and the Millennium Development Goals

## Growth and macroeconomic adjustment in developing countries<sup>8</sup>

The global economy is expected to recover, but only very gradually during 2013. While the road to recovery in advanced economies will remain bumpy, downside risks to the outlook have eased as policy intentions in advanced economies have become clearer and commodity price volatility has abated. While important downside risks remain—including, adjustment fatigue in advanced economies and overinvestment and high asset prices in emerging market and developing countries—overall risks are now more symmetric. In emerging market and developing countries economic activity is picking up, with activity in the advanced economies expected to follow later in the year. A broadly appropriate current policy stance in emerging market and developing countries is supporting continued strong growth in these countries, but some tightening of the policy stance appears appropriate over the medium term, beginning with monetary policy and prudential measures. Commodity prices trended down through most of 2012 and are expected to remain weaker in 2013, providing room for a flexible implementation of monetary policy, particularly in emerging market and developing countries.

Despite sustained economic growth, progress in rebuilding policy buffers in low-income countries has been modest. There are large differences across countries, however. Still high international commodity prices are providing commodity exporters with relatively larger buffers than commodity importing countries. The downside risk of a protracted global growth slow-down extending through 2015 would have a significantly negative impact on growth in low-income countries. With policy buffers not yet restored to levels preceding the 2009 crisis and against the backdrop of reduced traditional sources of financing, most low-income countries would likely need to undertake adjustments in the face of such a shock.

This year's Global Monitoring Report focuses on agglomeration as an important driver of development. As factors of production agglomerate they become more productive because it becomes easier to exploit economies of scale and scope. These economic aspects of agglomeration are most often looked at from a microeconomic perspective, but broad-based changes to where people work and live also have profound macroeconomic consequences. Using a World Bank agglomeration index, evidence is presented below suggesting that there are relatively higher returns to agglomeration on the lower rungs of development. Recent research at the IMF suggests that greater economic diversification is associated with improved macroeconomic performance. Another strand of research—that has benchmarked structural transformation in Africa with that of Asia's—provides some optimism with regard to Africa's economic prospects.

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<sup>8</sup> This draft chapter draws on the IMF's *World Economic Outlook Update* as of January 23, 2013. The final text will incorporate the revised projections included in the April 2013 *World Economic Outlook*.

## A modest uptick in global economic growth to provide renewed support toward achieving the MDGs

### Growth slowed in 2012, but should rebound in 2013

Global economic growth continued to slow in 2012 to 3.2 percent, from 3.9 percent in 2011 (Table 1.1). Growth slowed in advanced economies as well as in emerging market and developing countries, but the former group of countries grew significantly less than the latter group (1.3 percent and 5.1 percent respectively).<sup>9</sup> The growth slowdown in 2012 was somewhat more pronounced than foreseen in the *2012 Global Monitoring Report (GMR)*, mainly owing to lower than expected growth in emerging market countries. Importantly, however, the two country groupings most challenged in meeting the Millennium Development Goals (MDGs)—low-income countries and fragile states—both grew a robust 5.4 percent. The low and falling growth in the global economy was accompanied by low consumer price inflation in most countries and relatively stable international commodity prices.

There were large regional differences in growth performance across emerging market and developing countries in 2012. The recession in the euro area weighed heavily on Central and Eastern European countries. With Poland and Turkey tightening policies and several Southeastern European countries falling back into recession, growth in this region fell to just 1.8 percent. As in previous years, growth in emerging market and developing countries was led by those in Asia (6.6 percent). Bucking the trend, growth in the Middle East and North Africa countries recovered to 5.2 percent (from 3.5 percent in 2011), as these countries progressed in their political and social transitions, in particular in Libya (where GDP more than doubled after the economic collapse the year before). In Sub-Saharan Africa, robust growth continued in 2012, but the average growth rate of 4.8 percent masks large cross-country differences. Whereas conflicts negatively affected growth in Mali and Guinea-Bissau, growth in Cote d'Ivoire rebounded following the election-related disturbances in 2011. Despite the weaker overall economic outcome, per capita incomes rose in most countries (Figure 1.1).

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<sup>9</sup> The classification of countries is the one used in the IMF's *World Economic Outlook*. Emerging market and developing countries are those countries that are not designated as advanced countries. Countries that are eligible for financial assistance under the IMF's *Poverty Reduction and Growth Trust* constitute a subset of emerging market and developing countries; these countries are denoted low-income countries although eligibility is based on other considerations in addition to income levels. Emerging market and developing countries that are not eligible for financial assistance under the *Poverty Reduction and Growth Trust* are designated as emerging market countries. Fragile states are countries included in the World Bank's list of Fragile and Conflict-Affected States as of early 2013. Appendix Table 1 includes the list of all countries and economies.

**Table 1.1 Global Output**  
(Annual percent change)

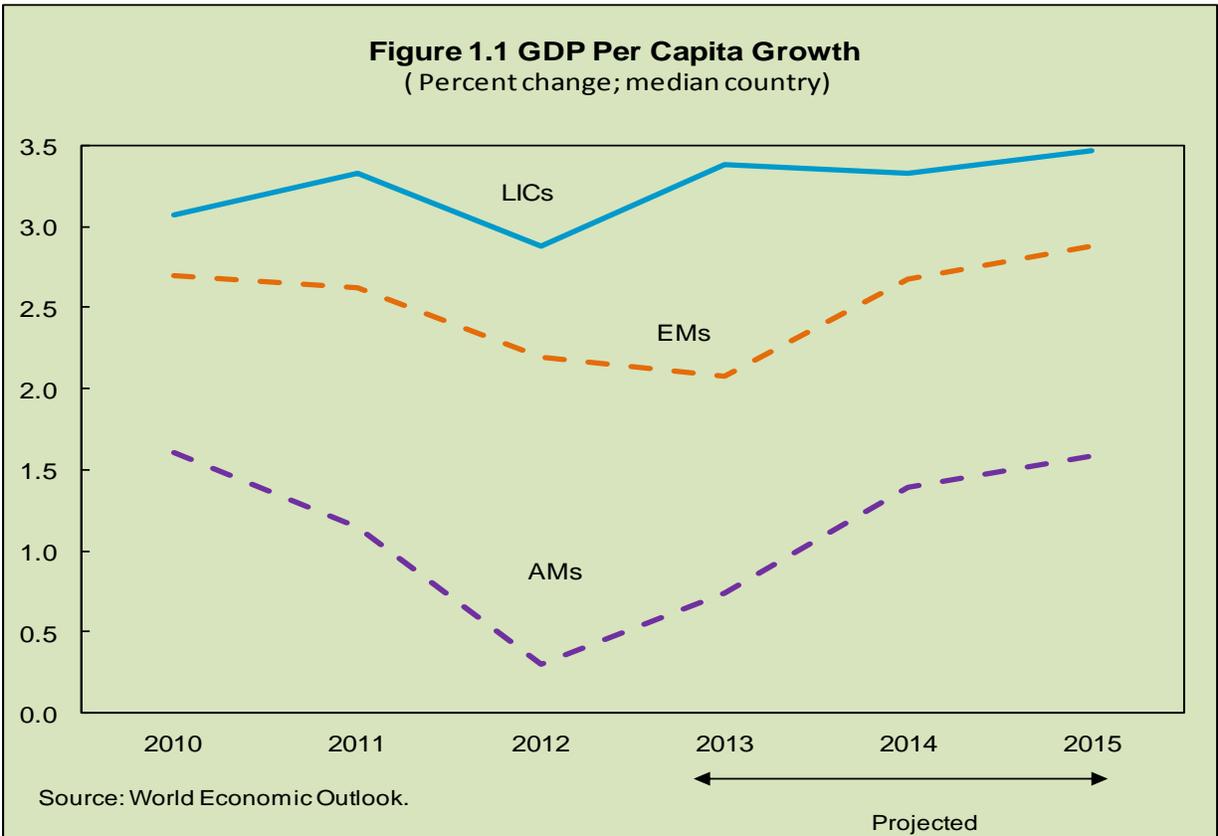
	2010	2011	2012	Projections		
				2013	2014	2015
<b>World</b>	<b>5.1</b>	<b>3.9</b>	<b>3.2</b>	<b>3.5</b>	<b>4.1</b>	<b>4.4</b>
Advanced economies	3.0	1.6	1.3	1.4	2.2	2.5
Emerging Market and Developing Countries	7.5	6.3	5.1	5.5	5.9	6.0
Central and Eastern Europe	4.6	5.3	1.8	2.4	3.1	3.5
Commonwealth of Independent States	4.8	4.9	3.6	3.8	4.1	4.1
Developing Asia	9.6	8.0	6.6	7.1	7.5	7.6
Middle East and North Africa	5.1	3.5	5.2	3.4	3.8	4.3
Sub-Saharan Africa	5.4	5.3	4.8	5.8	5.7	5.9
Western Hemisphere	6.1	4.5	3.0	3.6	3.9	3.9
Low-Income Countries <sup>1</sup>	6.3	5.6	5.4	6.1	6.3	6.6
Emerging Market Countries <sup>2</sup>	7.5	6.4	5.1	5.4	5.8	6.0
Fragile States <sup>3</sup>	4.4	3.2	5.4	7.1	6.7	6.9

<sup>1</sup>Low-income countries are those eligible for financial assistance under IMF's Poverty Reduction and Growth Trust, and Zimbabwe.

<sup>2</sup>Emerging market countries are emerging market and developing countries that are not low-income countries.

<sup>3</sup>A subset of emerging market and developing countries included in the World Bank's list of Fragile and Conflict-Affected States.

Source: World Economic Outlook.



The *World Economic Outlook* of the International Monetary Fund (IMF) foresees a gradual upturn in global growth during 2013, to 3.5 percent. The expected increase in growth is modest as the underlying fragilities that caused the slowdown in 2012 take time to unwind. The ongoing fiscal consolidation and financial sector deleveraging will continue to weigh on the euro area and its economy is projected to contract for a second year in a row. Other advanced economies are projected to expand, but growth will be held back by headwinds that include subdued external demand in, and financial spillover effects from, the euro area, and fiscal consolidation (e.g., in the United States). Overall, advanced economies are projected to grow 1.4 percent—about in line with the growth in 2012.

In the emerging market and developing countries, prospects are for a strengthening of growth to 5.5 percent in 2013. Growth is being supported by appropriate policies for the most part, but held back by weak demand in advanced economies. Lower commodity prices will also lead to terms of trade losses for commodity exporters, with knock-on effects on growth. Diminished policy space, policy uncertainty, and supply bottlenecks hamper growth in some countries (for example, India). As in 2012, the countries in central and eastern Europe and the Asian countries would be the slowest and fastest growing groups of countries (projected to grow by 2.4 and 7.1 percent respectively). The countries in central and eastern Europe—with their deep trade and financial links to western Europe—will continue to be negatively affected by spillovers from the euro area, while the strong growth in Asia is predicated on continued expansion in China and a strong recovery in India. Growth in the Middle East and North Africa will be modest reflecting ongoing political transitions and a slowdown among the region’s oil exporters.

Notwithstanding a somewhat weaker outlook for commodity prices, Sub-Saharan African economies are expected to expand by close to 6 percent.

Strong domestic government revenue mobilization is key to emerging market and developing countries having the resources needed to address their development challenges, including enhancing infrastructure provision and achieving the MDGs. In that regard, the 2009 global crisis was a major set-back as the crisis led to a 3 percentage point of GDP drop in revenues. Since then, revenues have recovered somewhat, but not fully, and are expected to remain below pre-crisis levels through 2015 (Table 1.2).

**Table 1.2 Government Revenue Excluding Grants<sup>1</sup>**

(Weighted averages, percent of GDP)

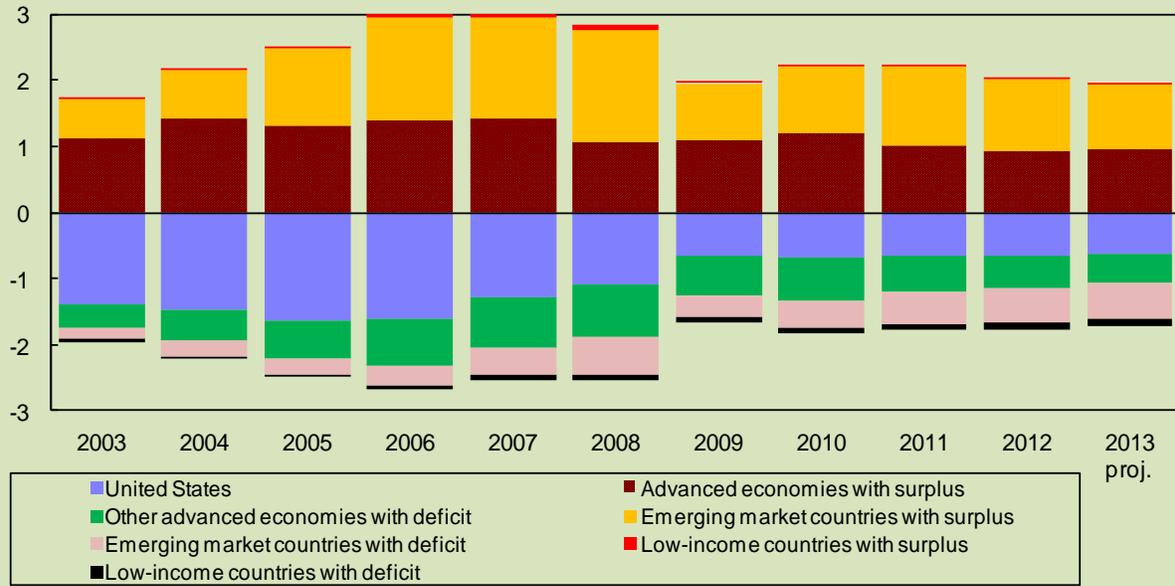
	2008	2009	2010	2011	2012	Projections		
						2013	2014	2015
<b>Emerging Market and Developing Countries</b>	29	26	27	28	28	28	27	27
Central and Eastern Europe	36	35	35	37	37	37	36	36
Commonwealth of Independent States	39	35	35	37	37	35	34	33
Developing Asia	20	20	21	22	22	22	22	22
Middle East and North Africa	43	34	35	39	38	38	37	36
Sub-Saharan Africa	28	23	24	28	27	26	26	25
Western Hemisphere	29	28	29	30	30	30	30	30
Low-Income Countries <sup>2</sup>	24	19	21	23	23	23	22	22
Of which: Fragile States <sup>3</sup>	22	17	19	20	20	21	20	20
Emerging Market Countries <sup>4</sup>	29	26	27	28	28	28	27	27

<sup>1</sup> General Government.  
<sup>2</sup> Low-income countries are those eligible for financial assistance under IMF's Poverty Reduction and Growth Trust, and Zimbabwe.  
<sup>3</sup> A subset of low-income countries included in the World Bank's list of Fragile and Conflict-Affected States.  
<sup>4</sup> Emerging market countries are emerging and developing countries that are not low-income countries.  
Source: World Economic Outlook.

Global current account imbalances—which widened in the run-up to the crisis—narrowed as the crisis hit and have since remained broadly stable (Figure 1.2). Robust net financial flows to emerging market and developing countries have also remained fairly constant from 2009 onwards, with prospects of no major changes for 2013 (Table 1.3). Emerging market countries receive on average about 7 percent of GDP in net financial flows, with most of these flows being private sector financial flows (including transfers). Relative to GDP, low-income countries receive net financial inflows that are about twice as high, averaging 14 percent of GDP in recent years. Relative to emerging market countries, low-income countries receive more private capital flows and private transfers, but the main factor behind the higher inflows to low-income countries is the significantly higher level of official inflows (capital and transfers). Fragile states receive significantly higher net inflows (relative to their GDP). In both 2011 and 2012, fragile states received net inflows that averaged close to 20 percent of GDP and the prospects are for a similar level of inflows in 2013.

**Figure 1.2 Global Current account Imbalances**

(In percent of World GDP)



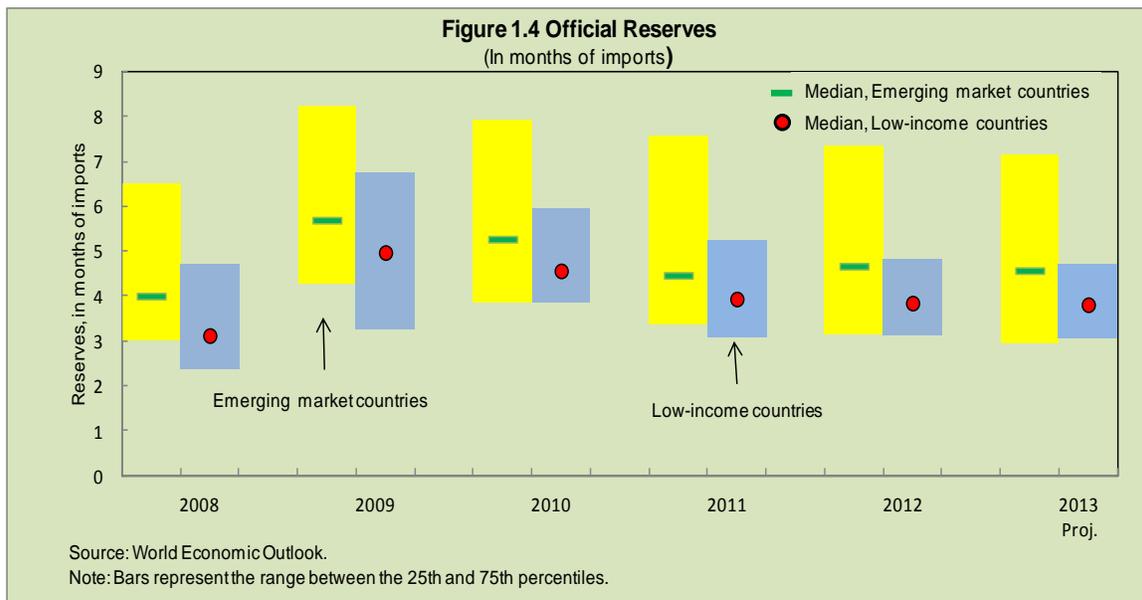
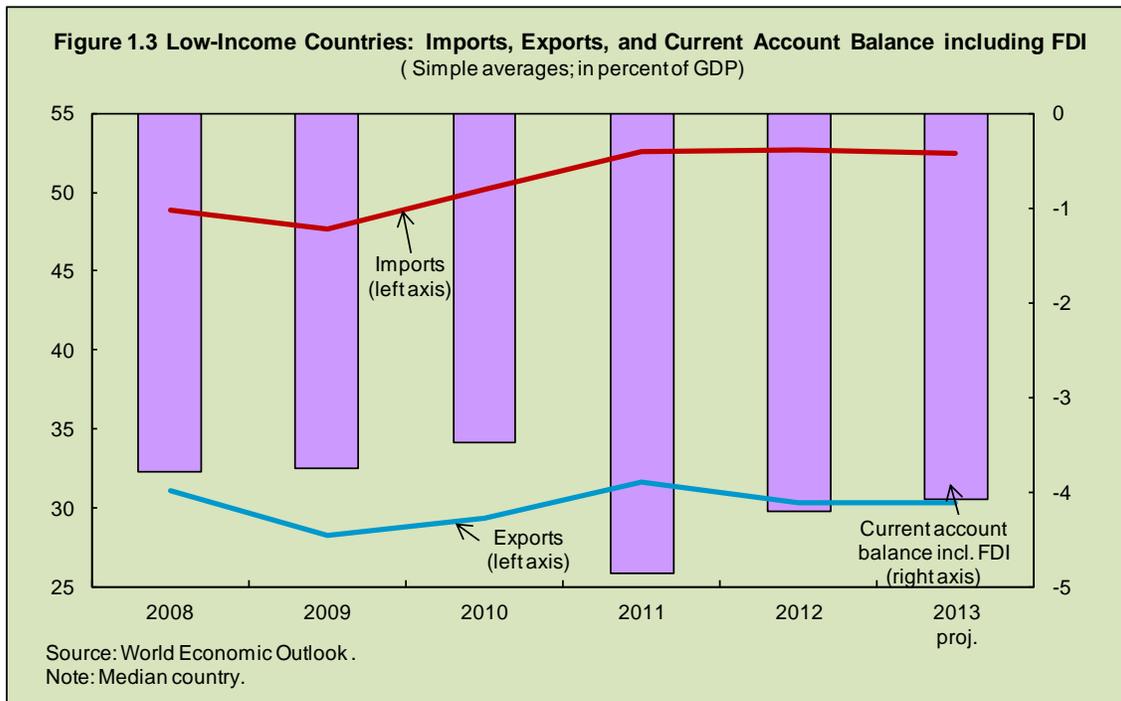
Source: World Economic Outlook.

**Table 1.3 Net Financial Flows**  
(In percent of GDP)<sup>1</sup>

	2008	2009	2010	2011	2012	2013 Proj.
<b>Emerging Market Countries</b>	9.0	7.3	7.6	7.2	6.7	7.0
Private capital flows, net	5.4	1.5	2.4	2.9	2.4	2.7
o/w: private direct investment	5.1	3.8	3.2	3.3	3.0	3.0
private portfolio flows	-1.2	-0.8	0.5	0.4	0.4	0.5
Private current transfers	3.5	3.5	3.5	3.3	3.4	3.3
Official capital flows and transfers (net)	0.1	2.4	1.7	1.0	0.9	0.9
Memorandum item:						
Change in reserve assets (–, accumulation)	-1.7	-2.8	-2.0	-1.4	-0.5	-0.9
<b>Low-Income Countries</b>	15.2	13.8	13.3	15.8	14.7	14.3
Private capital flows, net	4.6	3.3	3.8	4.7	3.6	3.9
o/w: private direct investment	6.6	5.3	5.8	6.5	5.6	5.7
private portfolio flows	-0.9	-1.0	-1.0	-0.7	-0.7	-0.7
Private current transfers	5.1	4.8	4.6	4.7	4.7	4.6
Official capital flows and transfers (net)	5.6	5.7	4.9	6.4	6.4	5.8
Memorandum item:						
Change in reserve assets (–, accumulation)	-2.2	-1.9	-1.6	-1.9	-1.1	-1.1
<b>Fragile States<sup>2</sup></b>	14.9	11.6	9.8	19.1	19.6	19.1
Private capital flows, net	4.5	3.3	2.8	5.3	6.0	6.5
o/w: private direct investment	4.3	3.3	3.8	5.3	4.9	5.1
private portfolio flows	0.2	-0.2	-0.3	-0.4	-0.3	-0.5
Private current transfers	5.9	6.1	5.8	6.0	5.8	5.7
Official capital flows and transfers (net)	4.4	2.2	1.2	7.9	7.8	6.9
Memorandum item:						
Change in reserve assets (–, accumulation)	-1.7	-1.6	-1.9	-1.9	-1.0	-1.3

Source: World Economic Outlook.  
<sup>1</sup>Equally weighted.  
<sup>2</sup>A subset of emerging market and developing countries included in the World Bank's list of Fragile and Conflict-Affected States.

World trade was stagnant in 2012, reflecting weak import demand in advanced economies and relatively stable international commodity prices. Emerging market and developing countries' trade expanded by 6 percent, down sharply from 22 percent the previous year (in nominal US dollars terms). In contrast, advanced economies' trade contracted by 1 percent. The typical low-income country is highly integrated into the world economy with import and export shares of GDP of about 50 and 30 percent respectively (Figure 1.3). The current account deficits (including foreign direct investments) in these countries were somewhat lower in 2012 than the previous year. These deficits remain higher than before the 2009 crisis and little change is expected for 2013. Official reserves, in months of imports—a standard measure of reserve adequacy for an emerging market or low-income country—changed little in 2012, reflecting modest increases in both imports and reserve accumulation (Figure 1.4). Less than a quarter of all emerging market and developing countries maintain reserves of less than three months imports.



### Macroeconomic policies

In 2012, the continuing challenge for policy-makers in most advanced economies was how concurrently to support a feeble recovery and address concerns about medium term fiscal sustainability. With inflation expectations well-anchored, monetary policy continued to remain supportive, while firm expenditure controls allowed room for a narrowing of fiscal deficits. Food and other commodity prices in global markets rose sharply from late 2010 to late 2011, followed by some pull-back through most of 2012

(Figures 1.5 and 1.6). In emerging market and developing countries, commodity price movements impact consumer prices, terms-of-trade, and income to a larger extent than in advanced economies. For that reason, commodity price volatility complicates macroeconomic policymaking in emerging market and developing countries.

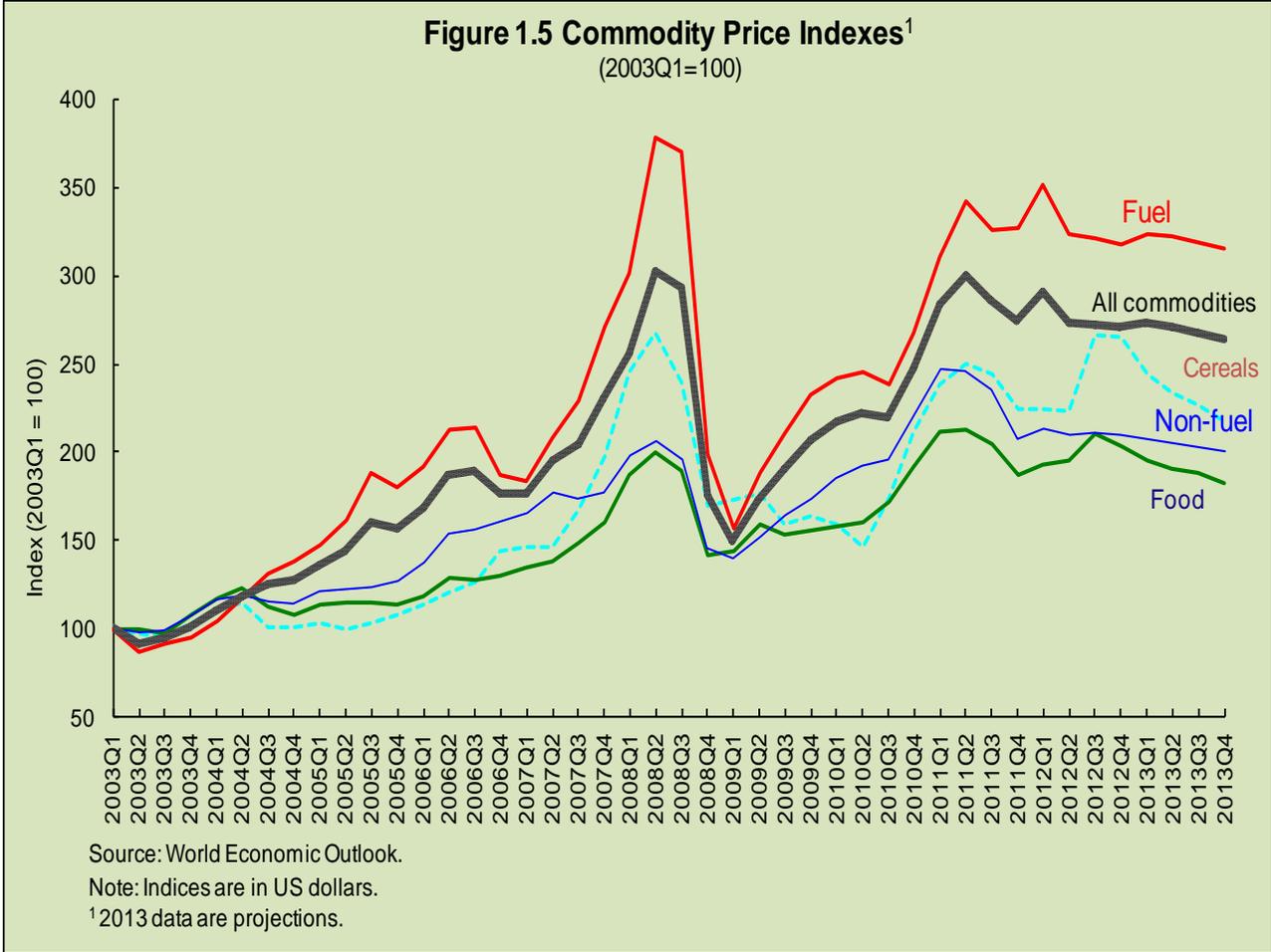
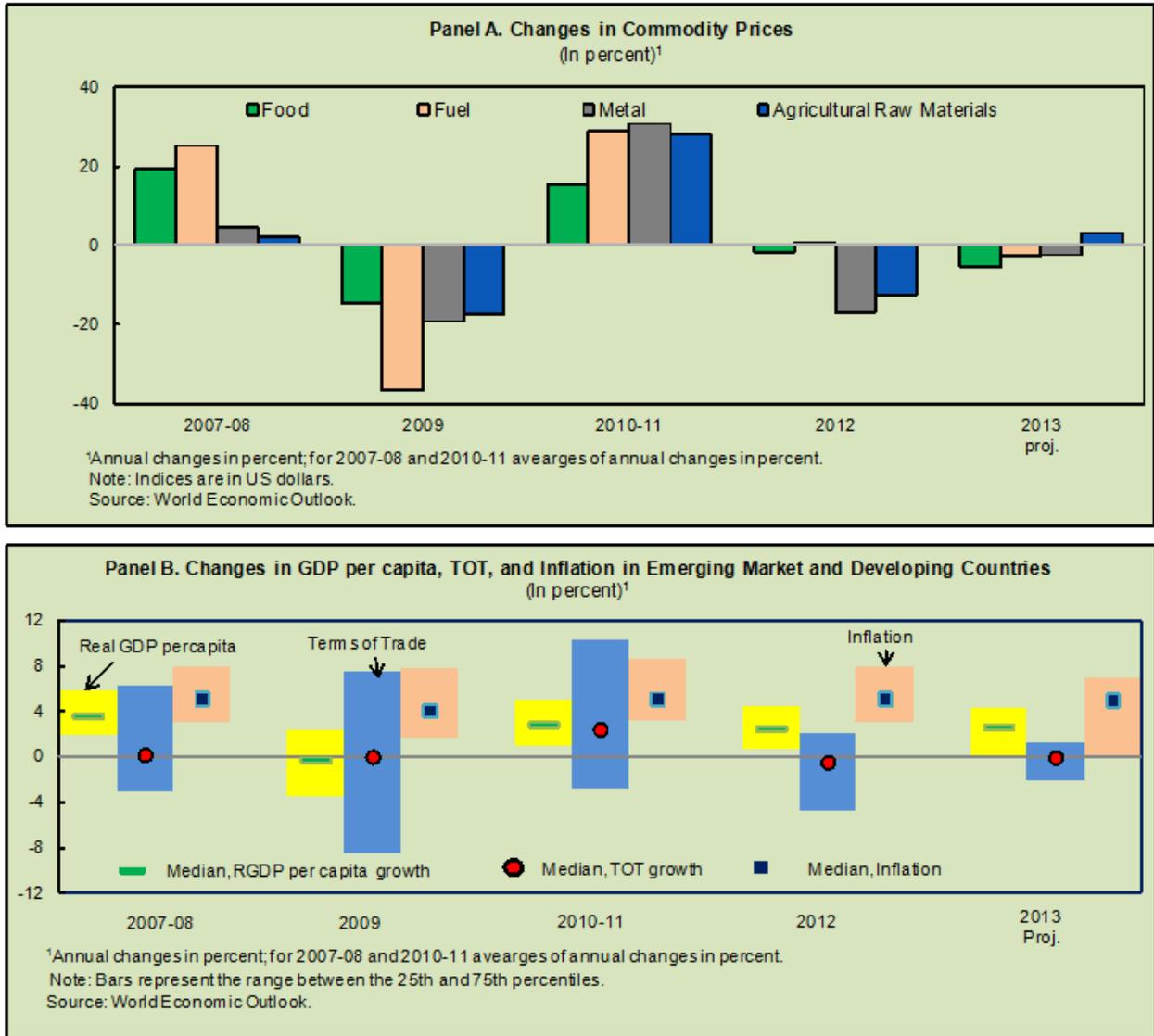
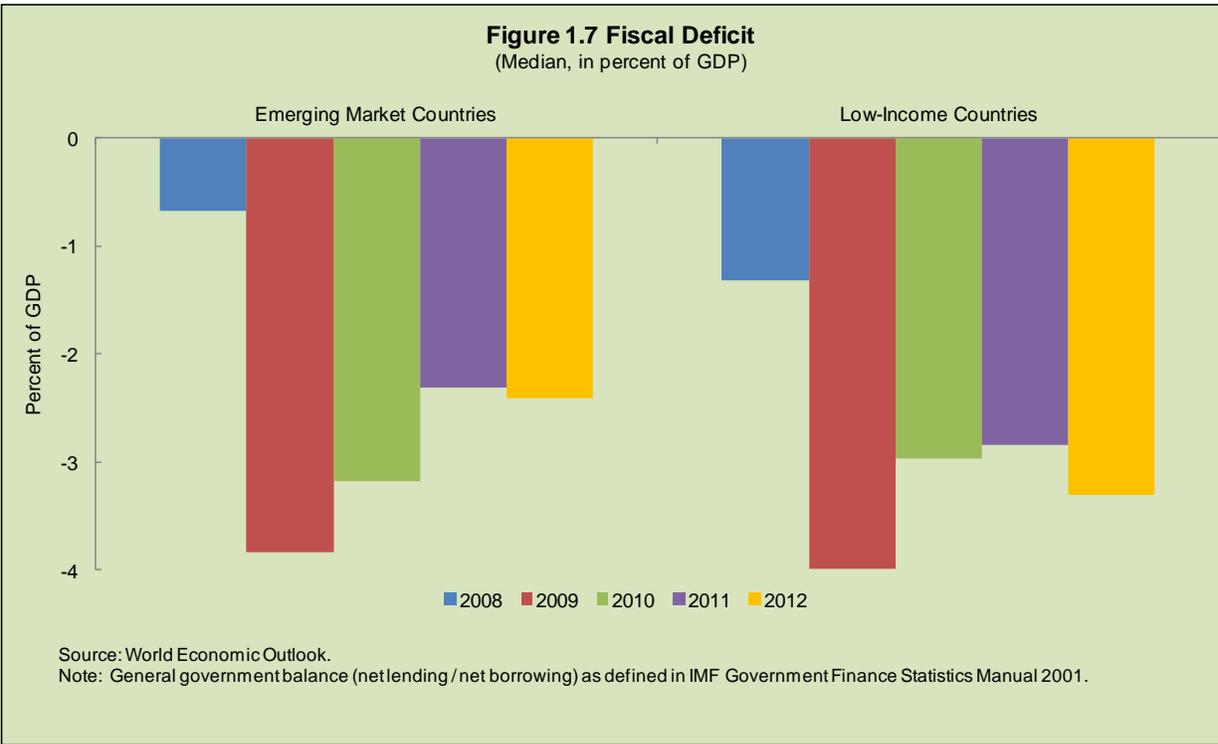


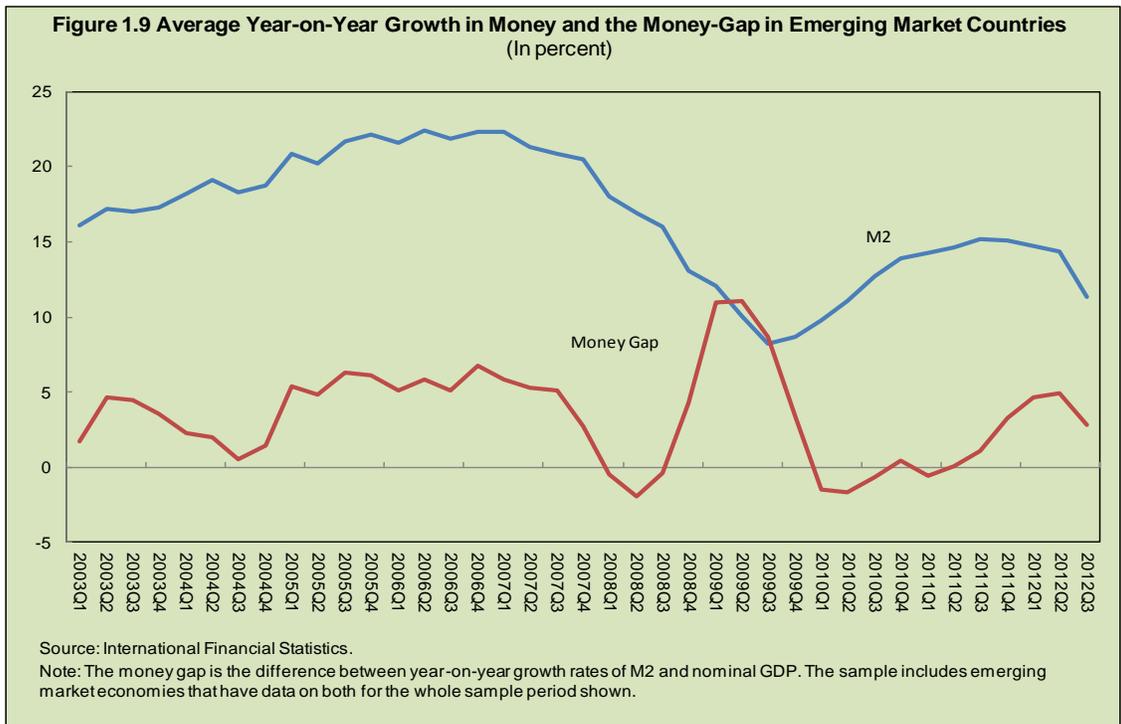
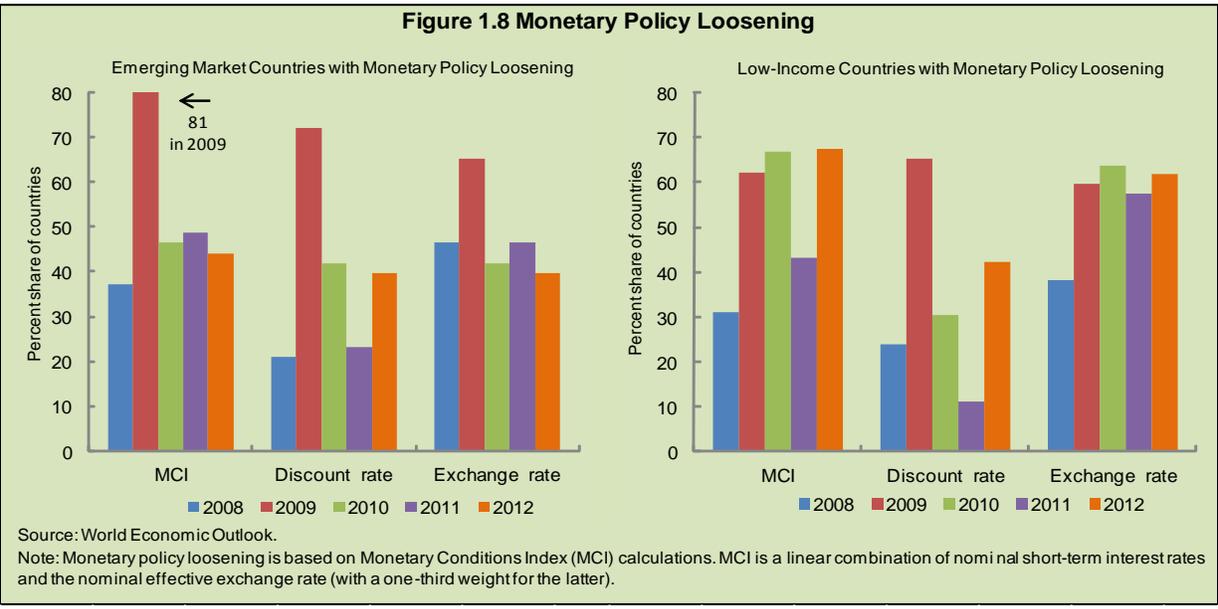
Figure 1.6



Fiscal deficits tended to widen in 2012 in both emerging market and low-income countries (Figure 1.7). Thus, the trend toward reinforcing fiscal buffers has stalled. In the 2009 crisis, large buffers made possible an unprecedented countercyclical fiscal response of the order of about 3 percentage points of GDP, but three years after the crisis less than half of this buffer has been reconstituted.

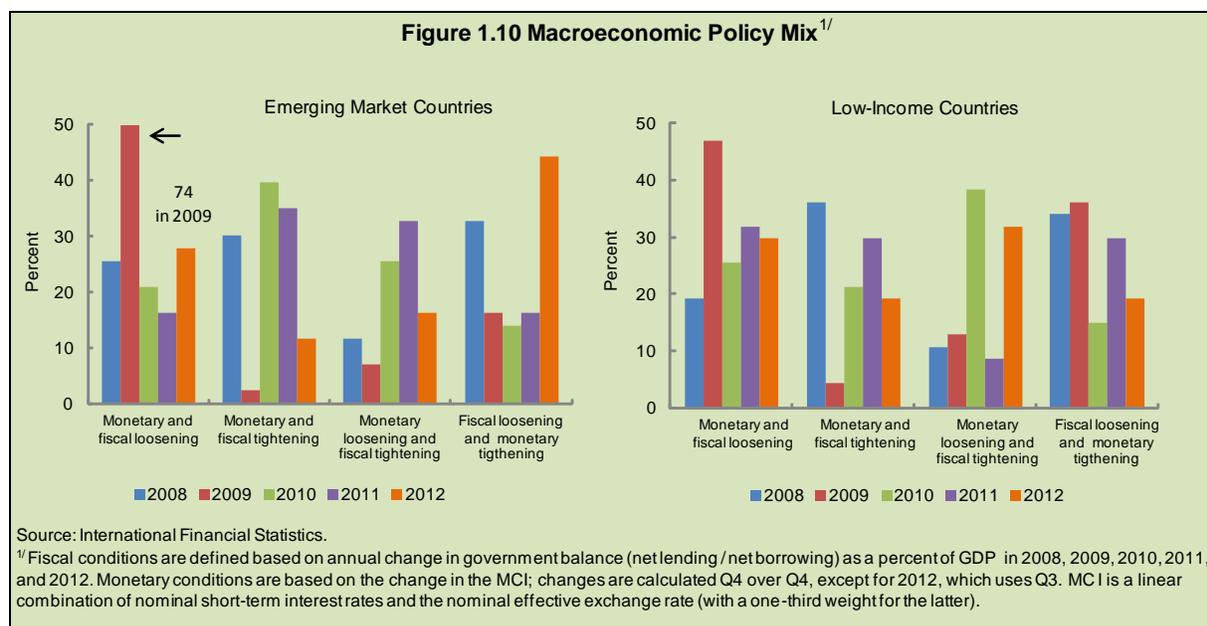


Slightly more than half of all emerging market countries continued to tighten monetary policy in 2012 (Figure 1.8). Among the countries that loosened monetary policy, the loosening took the form of reduced nominal short term interest rates and depreciation of the currency in about equal measure. In low-income countries, a significant majority of countries loosened monetary policy in 2012, in sharp contrast to 2011. In these countries, the monetary loosening mostly took the form of currency depreciation although the number of countries using the interest rate instrument increased significantly from 2011 to 2012. Against this background, growth in monetary aggregates relative to GDP in emerging market countries broadly reverted to trends prevailing prior to the 2009 crisis (Figure 1.9).



The macroeconomic policy mix varied sharply across emerging market countries and low-income countries in 2012; the mix also changed appreciably from 2011 to 2012 (Figure 1.10). About one-fourth of all countries loosened both monetary and fiscal policy in 2012 with significantly fewer countries tightening both types of policies. Thus, most countries did not unambiguously tighten or loosen the macroeconomic policy stance; rather they offset tightening of one kind of policy with a compensating

loosening of another kind of policy. Emerging market countries shifted markedly toward relaxing fiscal policy in 2012, with an offsetting tightening of monetary policy. In low-income countries the trend was in the opposite direction.



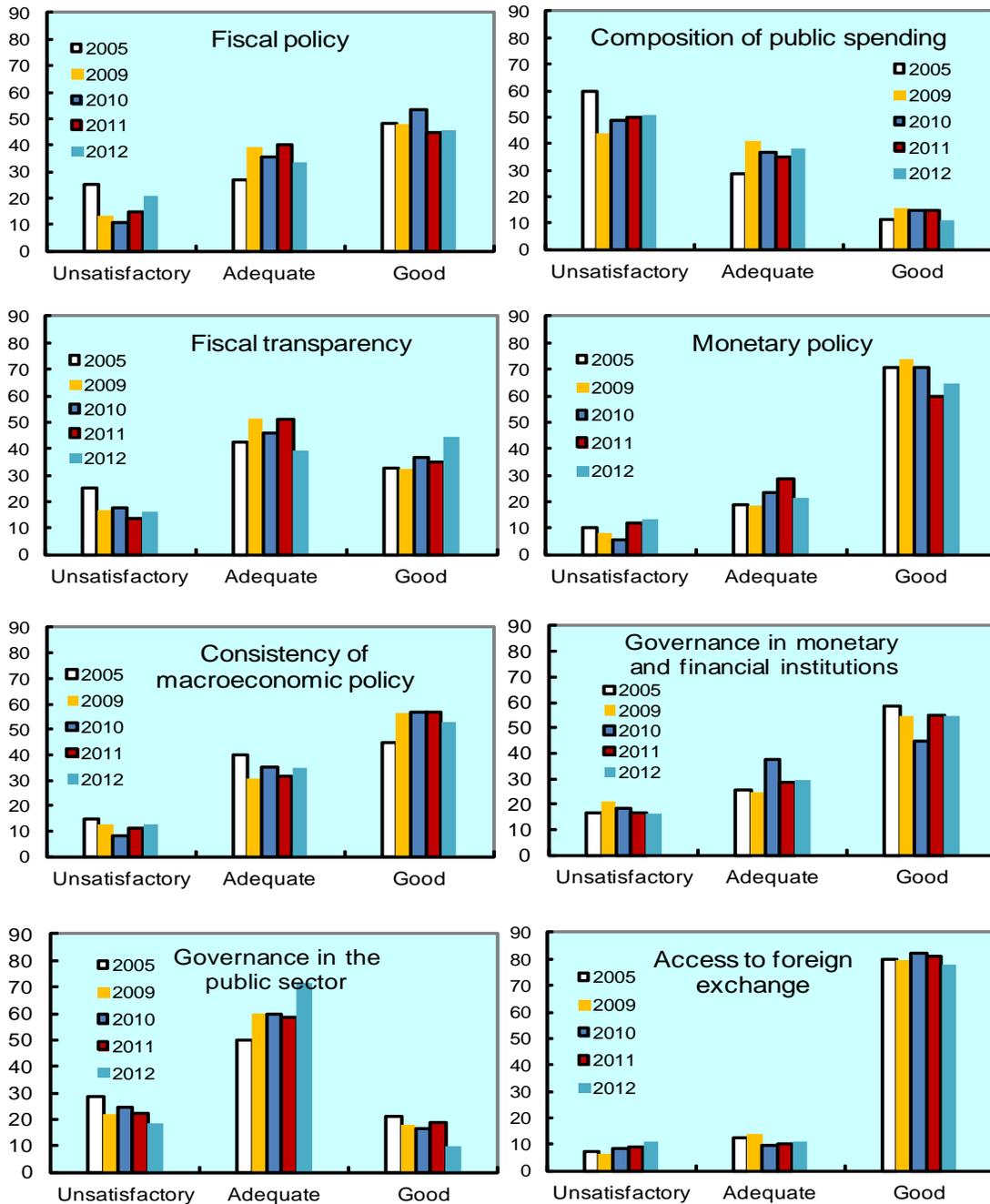
### Quality of macroeconomic policies in low-income countries

Since 2003, the quality of macroeconomic policies in low-income countries has been assessed through annual surveys of IMF country desks.<sup>10</sup> Over the years, significant progress has been made in several areas of economic policy. Low-income countries in Sub-Saharan Africa have registered relatively higher improvements. The number of countries with unsatisfactory policies has declined substantially since 2005 in most categories. However, there are substantial differences in the quality of policies across the different policy areas, with concerns typically focusing on fiscal issues (Figure 1.11). In 2012, the share of countries rated positively on the composition of public spending—an important driver for the attainment of the MDGs—reversed some of the modest gains achieved since 2005. In fiscal transparency, compared with 2011, a number of relatively strong-performing countries scored higher in 2012, while the number of countries with unsatisfactory policies relating to governance in the public sector declined. Monetary policy and governance of financial institutions continue to remain relatively strong areas of macroeconomic policies. The assessment of consistency of macroeconomic policies remains mixed. From 2011 to 2012, the number of countries with unsatisfactory policies increased slightly while the number of relatively strong-performing countries fell.

<sup>10</sup> Each low-income country has been assessed according to a common set of criteria. For example, a country with a large fiscal deficit and an unsustainable level of public debt would be judged to have an unsatisfactory fiscal policy stance.

**Figure 1.11 Quality of Macroeconomic Policies in Low-Income Countries, 2005 and 2009-12<sup>1</sup>**

(Percent shares of countries falling in each category)



<sup>1</sup>IMF staff have assessed each low-income country according to a common set of criteria. Policies are assessed as unsatisfactory, adequate, and good for this purpose. For example, a country with an unsustainable level of public debt and a large fiscal deficit would be judged to have an unsatisfactory fiscal policy.

Source: IMF staff estimates.

## Managing macroeconomic risks in low-income countries

Most low-income countries (LICs) recovered quickly from the 2009 crisis and have experienced strong growth since early 2010.<sup>11</sup> The continuing recovery was helped by deepening links with emerging markets, which complemented traditional export demand from advanced economies. In addition to the traditional trade channels, low-income countries have become linked to emerging markets through remittances and financial linkages.<sup>12</sup>

However, as noted above, despite sustained economic growth, the recent progress in rebuilding policy buffers has been modest for most LICs and has been partially reversed in some others over the past two years. The situation varies widely across different country groups (Figure 1.12). For example, commodity-exporting countries have relatively high external and fiscal buffers, while small countries seem to be in a somewhat worse position than the rest.<sup>13</sup> Greater emphasis on rebuilding buffers would position LICs better to protect spending levels and growth in the event of future shocks. At the same time, the rebuilding of buffers has to be balanced with the need to maintain adequate space for development-enhancing expenditure, particularly for infrastructure and other expenditures aimed at achieving the MDGs.

An analytical framework developed by the IMF that assesses LICs' vulnerabilities to global risks was used to simulate the impact of a protracted growth downturn – a tail-risk event driven by a slowdown in potential growth in advanced and emerging markets.<sup>14</sup> Under this scenario, relative to the World Economic Outlook baseline projection, global growth is assumed to be lower by 0.5 percentage points in 2013, by 1.7 percentage points in 2014, and by 2.0 percentage points in 2015. The weaker global growth is assumed to lead to weaker demand for commodities, which would depress oil and non-oil commodity prices.

The protracted global growth slowdown scenario is estimated to have a large negative impact on growth in LICs, which would get progressively worse over time. The impact stems from below-trend demand for LIC exports, as well as a reduction in remittances and FDI inflows to LICs, particularly from emerging markets. The cumulative output loss over the period 2013-15 in the median LIC could reach 3.2 percentage points, with output losses ranging from 1.9 to 5.7 points across all LICs.<sup>15</sup>

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<sup>11</sup> For the IMF's vulnerability exercise for low-income countries, Somalia and South Sudan have been excluded due to lack of data.

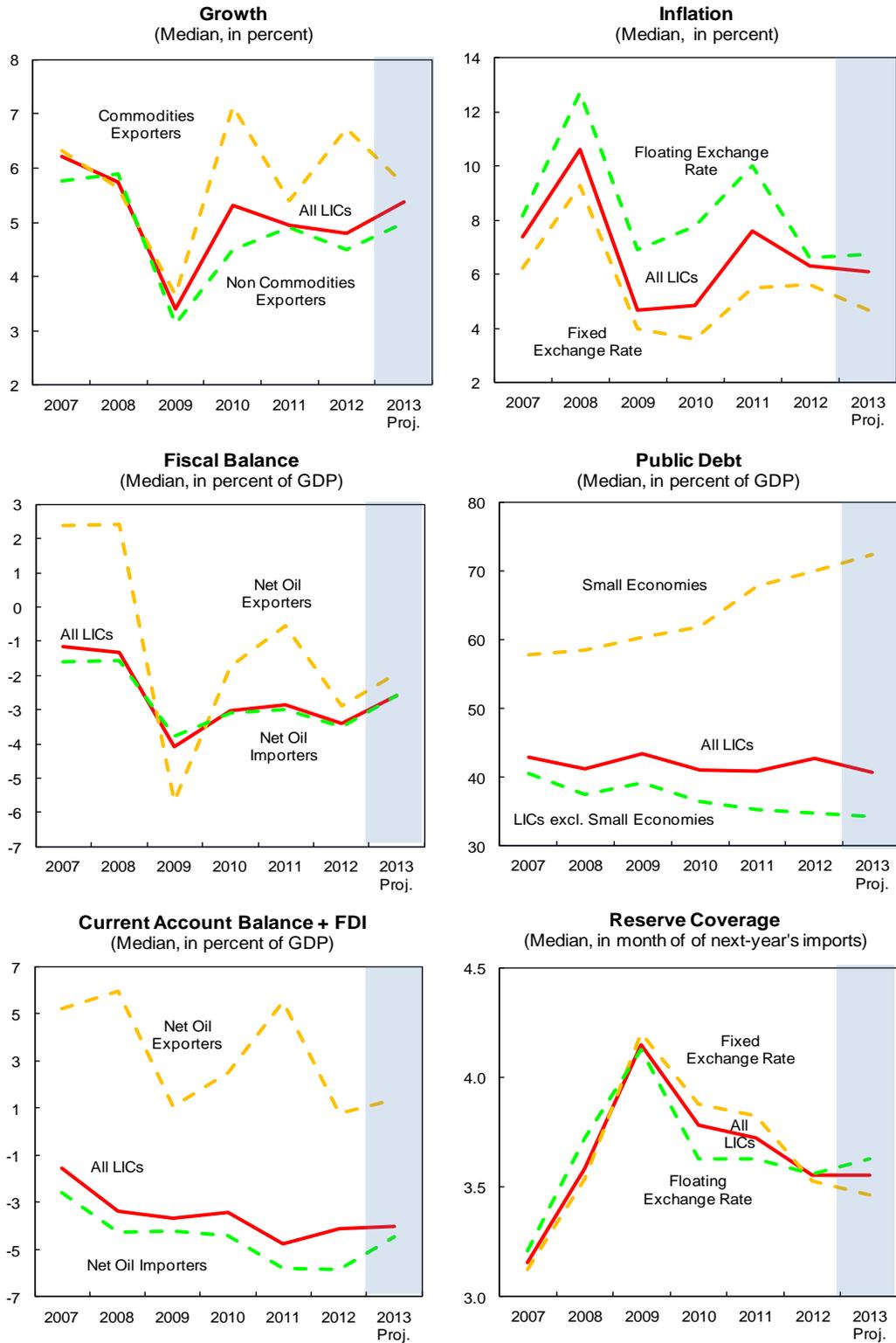
<sup>12</sup> See [Growth Drivers for Low-Income Countries—The Role of BRICs](#) (IMF, 2011a).

<sup>13</sup> Small low income countries are those with a population less than 1.5 million.

<sup>14</sup> See [Global Risks, Vulnerabilities, and Policy Challenges Facing Low-Income Countries](#) (IMF, 2012).

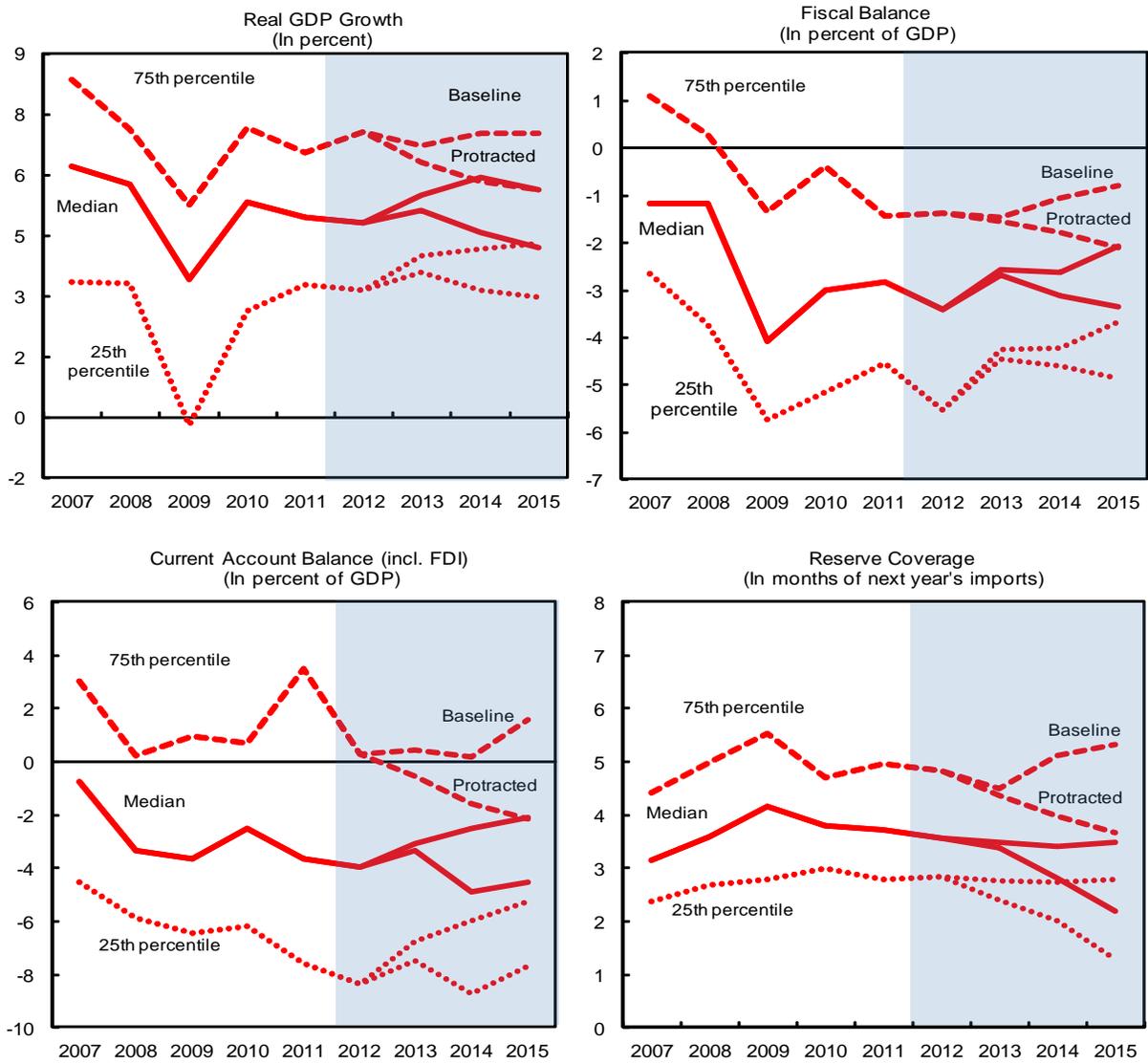
<sup>15</sup> All data under the vulnerability exercise refer to the median observation for 72 LICs, unless otherwise noted.

**Figure 1.12 Selected Macroeconomic Indicators for Low-Income Countries: 2007-2013**



Source: World Economic Outlook.

**Figure 1.13 Low-Income Countries: Impact of a Protracted Slowdown in Global Growth**



Sources: World Economic Outlook; and IMF staff estimates.

Under such a scenario, and before taking account of potential policy responses, fiscal and external buffers in LICs would progressively weaken as the permanent output loss accumulates over time (Figure 1.13). The cumulative widening in fiscal balances in 2013-15 in the median LIC could increase by 1.9 percentage points of GDP. This in turn could lead to significant public debt accumulation, compared to the gradual improvement in debt ratios projected in the baseline over the same period. Also, the cumulative deterioration in external balances would increase by 5.1 percentage points of GDP, resulting in sharp declines in reserve coverage across many LICs. Such imbalances could not be financed indefinitely. Additional cumulative financing needs could be as large as US\$26 billion by the end of 2014, cumulatively reaching about US\$61 billion by end-2015. This comes against the backdrop of reduced access to traditional sources of financing, reflecting budgetary pressures in donor countries. Therefore most LICs would most likely need to undertake medium-term adjustment in the face of such a protracted shock to global growth, while at the same time the IMF would likely be called upon to provide additional financial assistance.

If the risk of a protracted global downturn materializes, the appropriate policy response would need to reflect the permanent nature of the shock and the existing magnitude of policy buffers:

- *The magnitude of the required fiscal adjustment would depend on available fiscal space and debt sustainability.* Fragile LICs and those in Latin America and the Caribbean—especially small states that suffer from high debt and little, if any, fiscal space—may not have room for accommodative fiscal policy. LICs in Asia and the Pacific would have room for a small increase in deficits to accommodate the shock, given their stronger macroeconomic positions.<sup>16</sup>
- *The magnitude and timing of adjustment would also depend on growth prospects.* Countries with strong cyclical positions (high growth) but weaker macroeconomic positions would benefit from immediate adjustment. In contrast, a more gradual adjustment would be desirable in countries with a weak cyclical position (low growth), as rapid consolidation could depress growth and further weaken the fiscal position.
- *The composition of the adjustment would also need to strike a balance between revenue mobilization and expenditure measures.* Strengthening tax administration and avoiding ad hoc tax reductions would help limit the burden of adjustment falling excessively on the expenditure side and protect high priority expenditures (e.g., infrastructure and social sector spending). Making budgetary spending more growth-friendly (e.g. by reallocating spending from untariffed subsidies to productive investments) would improve the quality of adjustment and support domestic demand.

Optimally, fiscal adjustment should also be complemented by adjustment in monetary and exchange rate policies, and include some important structural measures. The majority of LICs would have sufficient policy space to reduce interest rates in response to a protracted global growth slowdown, as weaker domestic demand and commodity prices would lead to moderation in inflation. Some external adjustment could be also implemented, in particular in countries with overvalued exchange rates. In addition, some adjustment in private sector behavior would also help to partially offset the impact of lower external

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<sup>16</sup> Fiscal consolidation would also be needed in some resource-rich countries to build buffers over time that would help manage challenges arising from volatility and exhaustibility of natural resources.

demand by reducing imports to be consistent with the new weaker economic growth path and lower relative prices. The implementation of structural reforms could include measures to deepen the financial sector and develop domestic debt markets, coupled with strengthening the supervisory framework, as well as better-targeted investments in infrastructure to increase productivity and living standards.

## **Economic diversification and structural transformation**

The theme of this year’s Global Monitoring Report is *Rural-Urban Dynamics and the Millennium Development Goals*. Agglomeration is an important driver of development: as factors of production agglomerate—i.e., become geographically more concentrated—they become more productive because it becomes easier to exploit economies of scale and scope (*The Growth Report*, 2008). Network effects and other positive externalities in turn also positively impact productivity and economic growth. While agglomeration can be immensely beneficial, there are constraints: increasing congestion costs can provide a powerful check on any such process.

Agglomeration is part of a broader set of changes—including, for example, the demographic transition—that together constitute the transformation of traditional low-productivity economies into modern high-productivity economies. This transformation also typically encompasses the structural shift to manufacturing and service activities from agriculture. This section includes three different takes on the agglomeration process through a macroeconomic prism. The first explores to what extent differences in the degree of agglomeration across countries can provide insights into differences in macroeconomic outcomes such as growth. The latter two address, respectively, economic diversification in low-income countries and structural transformation in Sub-Saharan Africa.

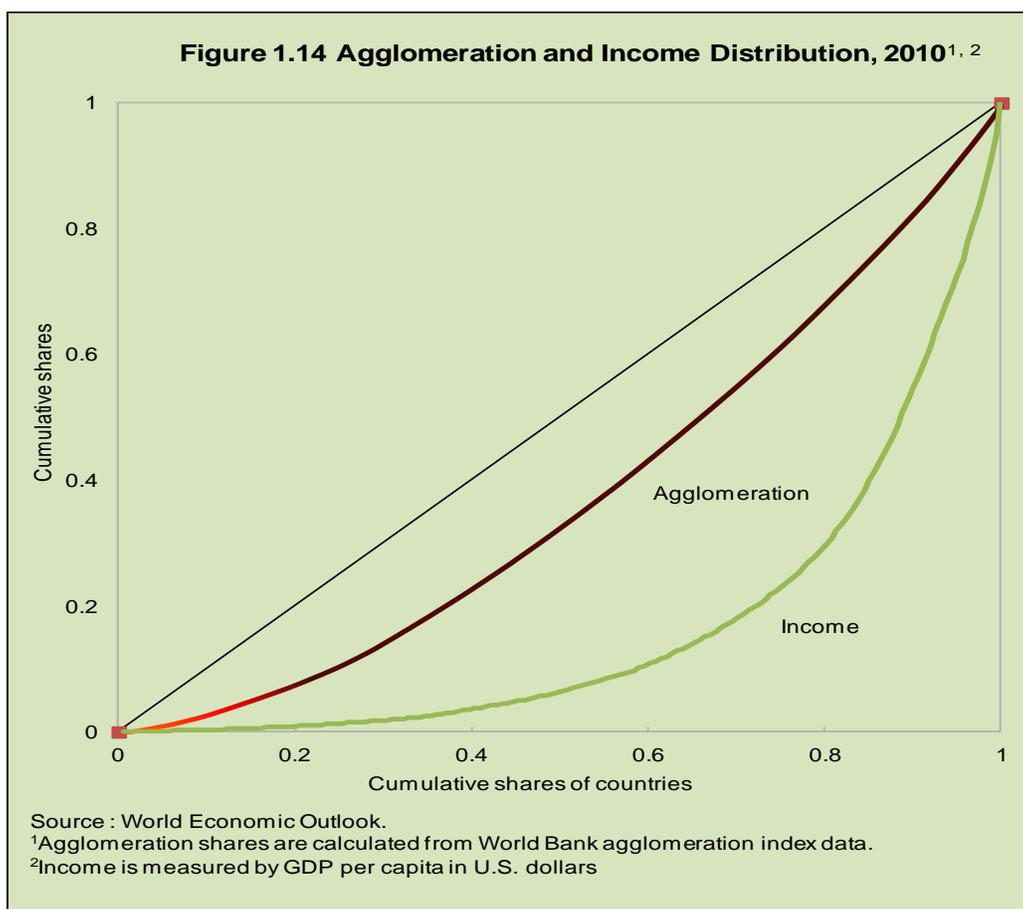
### **Macroeconomic performance and agglomeration**

For the *2009 World Development Report*, Bank staff developed an index that measures on a uniform basis country-specific levels of agglomeration.<sup>17</sup> A recent update of the index provides a snapshot of the degree of agglomeration in 162 countries in 2010. The combined population of the countries for which data are available is 6.8 billion (98 percent of the world’s population). The index ranges from a 7 percent urban population share in Papua New Guinea to a 100 percent urban population share in Singapore. The population-weighted average urban population share is 54 percent.<sup>18</sup> The distribution of countries thus designated is shown in Map 1.1 together with a corresponding relative income distribution of countries (using the same methodology).

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<sup>17</sup> The index uses a globally-consistent definition of settlement concentration based on population density, the population of a “large” urban center and travel time to that large urban center.

<sup>18</sup> In comparison, the United Nations’ *World Urbanization Prospects, the 2011 Revision*, April 2012 estimates the average urban population share to be 52 percent in 2010. The United Nations database is a more comprehensive and detailed data source; however, the definition of urbanization is not necessarily the same across countries.



The distribution of the degree of agglomeration across countries is highly uneven, but less so than that of income owing to the fact that the share of population living in urban areas cannot exceed 100 percent whereas there is no upper limit to income levels (Figure 1.14). As would be expected, there is a positive and statistically significant correlation between the degree of agglomeration and the level of per capita income. The Pearson and Spearman rank correlation coefficients between the two variables are 0.52 and 0.72 respectively (both statistically significant at the 5 percent level). This positive correlation should, of course, not be interpreted to mean that there is a causal link from agglomeration to income (or vice versa), but rather that a broader underlying development process impacts both agglomeration and income outcomes.

To further explore the interrelationship between countries' level of agglomeration and level of economic development, countries are divided into low-, medium-, and high-agglomeration countries respectively using the methodology of Nielsen (2011 and forthcoming).<sup>19</sup> Countries with an agglomeration share of 40 percent or lower (64 percent or higher) are designated as low-agglomeration (high-agglomeration)

<sup>19</sup> The methodology provides a way to construct a linear approximation of a Lorenz curve such that the difference between the linear approximation and the actual Lorenz curve is minimized. The linear segments represent different categories of countries; in this application, low-, medium-, and high-agglomeration countries.

countries. Medium agglomeration countries are countries with an urban population share of between 40 and 64 percent.

There is a large degree of overlap between the categorization of countries as low-, medium-, and high-agglomeration countries and the analytical country categorization of low-income, emerging market, and advanced economies (Table 1.4).<sup>20</sup> Most LICs are low-agglomeration countries and most advanced economies are high-agglomeration economies. Among emerging market countries about half are medium-agglomeration countries. The correlation between the two country classification systems is statistically significant<sup>21</sup>. Per capita income increases with the level of agglomeration for both low-income and emerging market countries, but the relative increases are more pronounced for LICs. Among advanced economies, there is no “return” to agglomeration (the higher per capita income level of the small group of medium-agglomeration advanced economies is because most Nordic countries are included here). These findings suggest that the positive correlation between agglomeration and development is more strongly felt in the poorer countries that are most challenged in attaining the MDGs.

	LIC	EM	AM	Total
<b>Number of countries</b>				
Low agglomeration countries	44	13	0	57
Medium agglomeration countries	20	42	9	71
High agglomeration countries	9	28	23	60
Total	73	83	32	188
<b>Population (in millions)</b>				
Low agglomeration countries	751	108	0	858
Medium agglomeration countries	545	4,007	57	4,610
High agglomeration countries	34	493	942	1,469
Total	1,330	4,608	999	6,937
<b>GDP per capita (in US dollars)</b>				
Low agglomeration countries	1,077	5,274	...	1,818
Medium agglomeration countries	1,396	7,004	43,411	10,320
High agglomeration countries	4,489	14,972	39,352	23,018
Total	1,599	9,847	40,459	12,193

Sources: United Nations Population Division, and World Economic Outlook.

<sup>20</sup>Member countries as of early 2013. For the 26 countries for which no agglomeration data are available, countries were assigned agglomeration status based on heuristic comparisons with like countries. GDP per capita income estimates exclude ten countries owing to lack of data.

<sup>21</sup>The Spearman rank correlation coefficient is 0.58 (statistically significant at the 5 percent level).

**Table 1.5 Average Real GDP Per Capita Growth, 2003-12<sup>1</sup>**

(In percent)

	Low Agglomeration Countries	Medium Agglomeration Countries	High Agglomeration Countries	All Countries
<b>World</b>	<b>3.1</b>	<b>3.5</b>	<b>2.2</b>	<b>3.0</b>
Advanced economies	...	1.2	1.3	1.2
Emerging and Developing Countries	3.1	3.9	3.0	3.4
Central and Eastern Europe	...	3.7	3.2	3.7
Commonwealth of Independent States	...	6.5	6.4	6.5
Developing Asia	4.7	5.6	3.3	5.0
Middle East and North Africa	0.6	2.6	2.9	2.6
Sub-Saharan Africa	2.7	2.1	3.6	2.6
Western Hemisphere	1.5	3.1	2.3	2.6
Low-Income Countries <sup>2</sup>	3.0	2.8	5.5	3.1
Fragile States <sup>3</sup>	1.8	0.7	.	1.7
Emerging Market Countries <sup>4</sup>	3.4	4.5	2.7	3.7

<sup>1</sup>For 162 countries for which data on the agglomeration index are available.

<sup>2</sup>Low-income countries are those eligible for financial assistance under IMF's Poverty Reduction and Growth Trust, and Zimbabwe.

<sup>3</sup>A subset of low-income countries included in the World Bank's list of Fragile and Conflict-Affected States.

<sup>4</sup>Emerging market countries are emerging market and developing countries that are not low-income countries.

Source: World Economic Outlook.

Looking at economic growth over the last ten years through the prism of agglomeration, growth in medium-agglomeration countries has outpaced that of both low- and high-agglomeration countries (Table 1.5). Given the large degree of overlap between countries categorized according to their level of agglomeration or development, this is not a surprising result (compare Table 1.5 with Table 1.1 and Figure 1.1).

Of more interest is therefore to compare macroeconomic outcomes across levels of agglomeration within different geographical areas. For example, growth in low- and medium agglomeration emerging market and developing countries in Europe and Asia has been higher than growth in similar high-agglomeration countries. For emerging market and developing countries in Africa, the Middle-East, and Western Hemisphere, the opposite result holds. In these regions, high-growth countries were for the most part high-agglomeration countries.

Turning to LICs, average annual per capita economic growth in 2003-12 in high-agglomeration countries was 5.5 percent annually, as compared with 3.0 percent and 2.8 percent respectively in low- and medium-agglomeration countries. The large differences in growth outcomes between high-agglomeration LICs, on the one hand, and low- and medium-agglomeration LICs, on the other hand, are statistically significant

(Table 1.6). In contrast, the difference in growth outcomes between low- and medium-agglomeration LICs (0.2 percent) is not statistically significant.

**Table 1.6 Statistical Tests for Mean-differences**

Mean Differences Between	LICs	EM	AM	Total
Low/High Agglomeration Countries	S	N	-	S
Low/Medium Agglomeration Countries	N	N	-	N
High/Medium Agglomeration Countries	S	S	N	S
Source: IMF staff estimates.				
Notes: S: Statistically significant; N: Not statistically significant.				

Agglomeration is an important aspect of development, but it is usually looked at from a microeconomic perspective. However, agglomeration differences across countries can provide additional insights into macroeconomic performance. The evidence presented here suggests that there are high returns to agglomeration, particularly for countries on the lower rung of development. For countries on higher rungs, the relative benefits and costs of concentrating people and other economic factors of production in urban settings is less clear cut.

### **Economic diversification in low-income countries**

Limited diversification in production is an underlying characteristic of many LICs. As countries grow, their economies often become more diverse, but only up to a point: at higher income levels economies again become less diverse. Low levels of diversity in LIC economies can reflect a broad range of market and government failures, and the result can be concentration in sectors with limited scope for productivity growth and quality upgrading, such as primary commodities. In turn, this can lead to less broad-based and sustainable growth, as well as increased exposure to adverse external shocks and macroeconomic instability.

A recent IMF *Staff Discussion Note*<sup>22</sup> sheds more light on the role of diversification in the macroeconomic performance of LICs, examining diversification not just in trade, but also in the broader domestic economy. Using existing data, as well as a new IMF cross-country dataset covering output in 12 sectors, and several new country case studies, this work reviews and extends the evidence pointing to diversification as a crucial aspect of the development process.

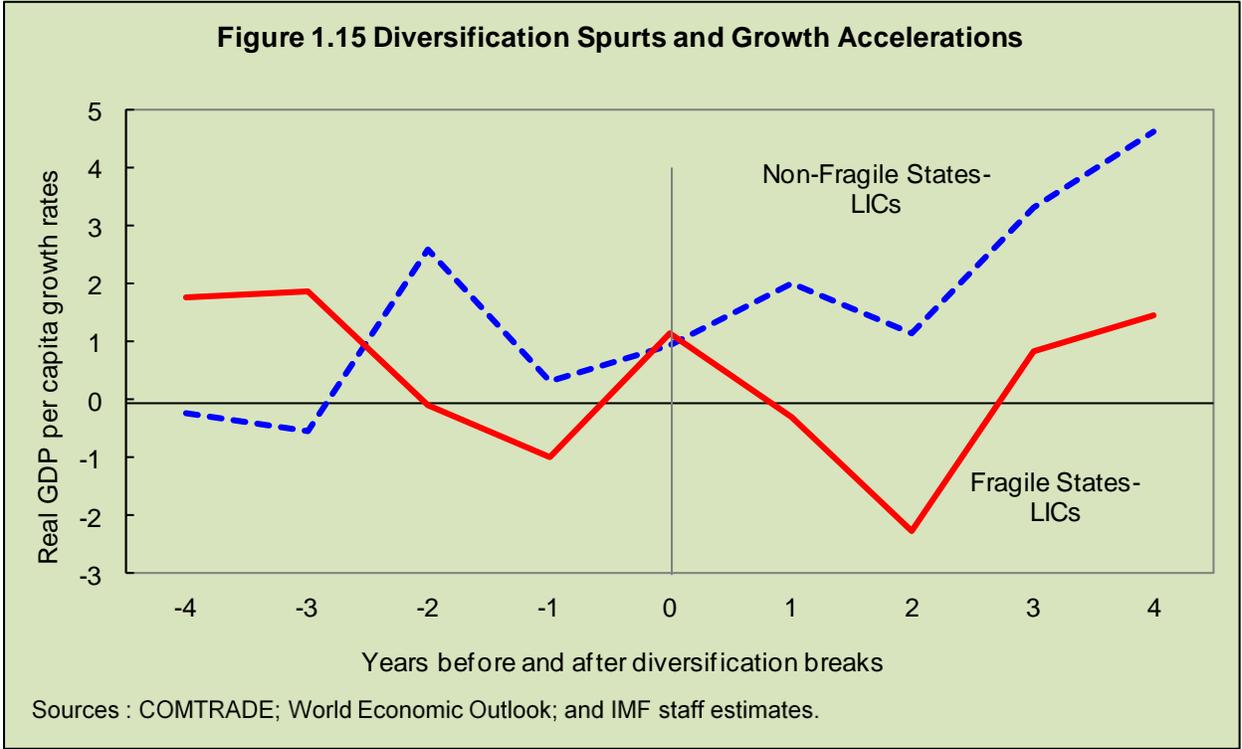
For an extended period, many LICs enjoyed little success in diversifying exports and production. The situation broadly improved after the mid-1990s, with significant changes in both the type and quality of goods produced and exported. However, there were major differences across regions and countries in the degree to which they succeeded in carrying out this economic transformation. In particular, sub-Saharan Africa currently stands out as far less diversified and as producing relatively lower quality goods than Asia.

<sup>22</sup> Papageorgiou, C., and N. Spatafora. 2012. “Economic Diversification in LICs: Stylized Facts and Macroeconomic Implications,” IMF *Staff Discussion Note* SDN 12/13.

Greater diversification is associated with improved macroeconomic performance, including both lower volatility and higher growth. “Diversification spurts”, that is, episodes of rapid, sustained diversification, are associated with a 17 percent average reduction in the volatility of output growth in developing countries, and a 30 percent decrease in output volatility in LICs.

Analogously, diversification spurts are associated with sharp subsequent accelerations in growth. This is especially true for non-fragile LICs (Figure 1.15). More broadly, initial diversification is on average positively associated with subsequent growth, although there is much cross-country heterogeneity.

This raises a key policy question: what factors can spur or, alternatively, impede diversification? Both policy and institutional factors can influence the transition to more diverse production structures, and thereby affect the pace at which growth can be sustained. For instance, policy barriers and structural rigidities in labor and product markets, or underdeveloped financial systems may hamper the process of diversification. Likewise, insufficient or low-quality public infrastructure may retard the development of those sectors that rely disproportionately upon it; this factor may prove especially important in LICs, where a large portion of investment stems from the public sector.



Case studies provide some tentative evidence in favor of three main themes. First, diversification and structural transformation are often underpinned by reforms and policy measures that are general in scope. Macroeconomic stabilization is a clear example. But even microeconomic measures are often broad-based, focusing on improving the quantity and quality of infrastructure or essential business services, or on setting up a welcoming environment for foreign investors. It remains an open issue to what extent industry-focused and narrowly targeted measures have historically helped underpin diversification efforts.

Second, effective policy measures come in “waves” and aim at exploiting the evolving comparative advantages of the economy in changing external conditions. The types of reforms underpinning diversification and structural transformation in the early stages of development are different from those required later on. In general, reforms need to be adapted to the external environment faced by the economy.

Finally, the frequency with which new products are introduced and the rate at which they grow can point to potential policy-driven bottlenecks. Little entry may indicate that barriers deter firms from exporting or experimenting. If survival rates are low, firms may face more obstacles than expected. If surviving firms cannot expand, they may have inadequate access to finance.

### **Structural transformation in Sub-Saharan Africa**

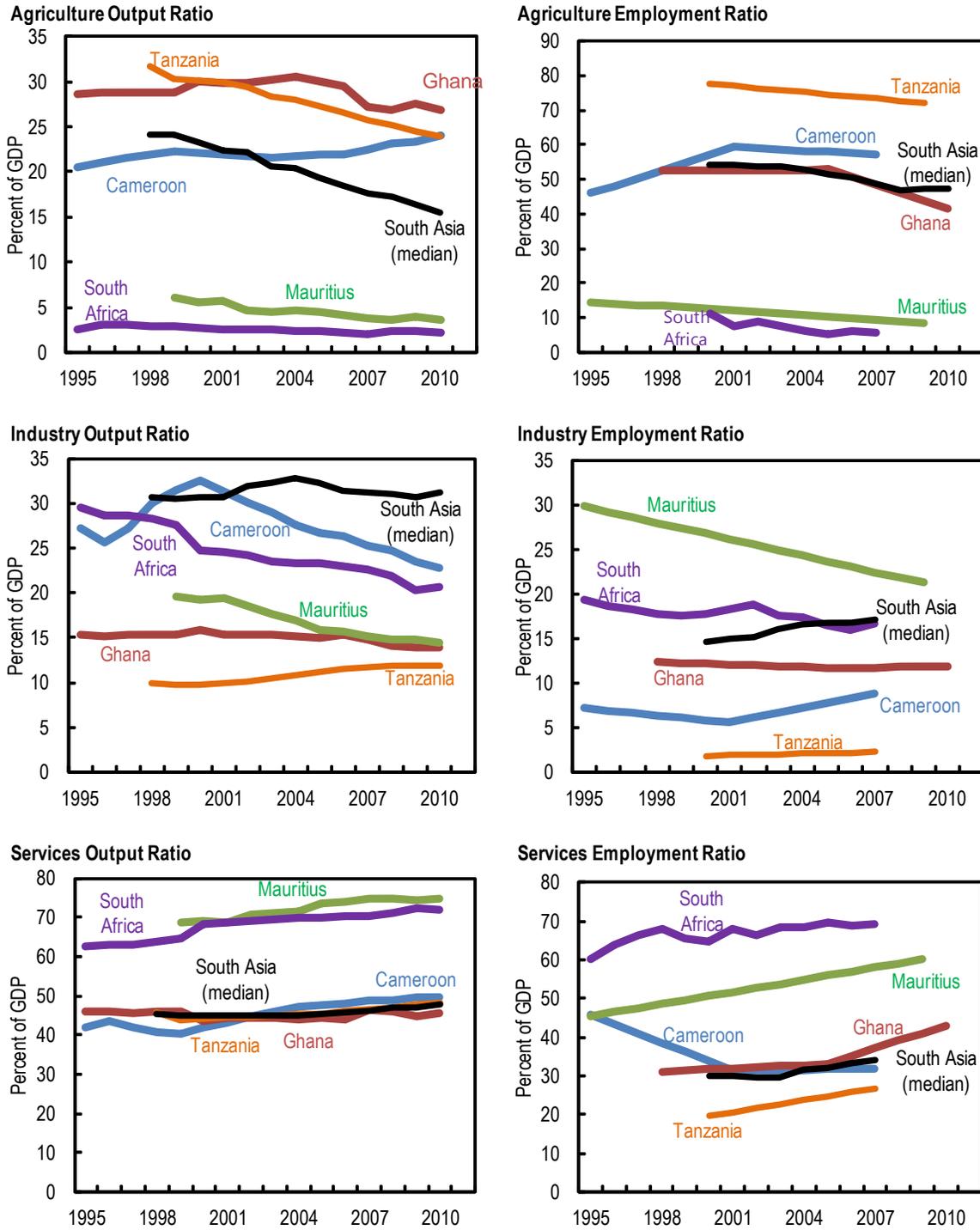
Sub-Saharan Africa (SSA) has been experiencing an episode of high growth since the mid-1990s. Many of the countries have benefited from relatively high commodity prices. One key question is whether higher growth has been accompanied by structural transformation, defined as the pattern of change in economic activity across sectors—from the primary to secondary and tertiary sectors—and across space—from rural to urban areas.

The IMF’s *Regional Economic Outlook: Sub-Saharan Africa* (2012) analyzes the former dimension of structural transformation, namely, whether growth has been accompanied by the shift of workers from low to high average productivity activities and sectors. Since on average more than half of the labor force is employed in agriculture in SSA economies, and agriculture accounts for about one third of output, average labor productivity in the sector is very low. Thus, structural transformation in SSA typically involves increasing the productivity of the agricultural sector, which frees up labor, allowing the shift of agricultural workers to industry and services.

Using data from 1995 to 2010 on agricultural output from the Food and Agricultural Organization (FAO) of the United Nations, GDP by sector from the IMF, and employment by sector from household surveys, the analysis of average labor productivity and the shift of workers across sectors shows that most countries in the region have experienced some degree of structural transformation, although there has been significant variation in its speed and type. In particular, transformation in SSA has been slower than that experienced by several countries in Asia: many SSA countries have experienced relatively slow productivity growth in agriculture and a less-pronounced shift from agriculture to services and, to an even lesser extent, to manufacturing.

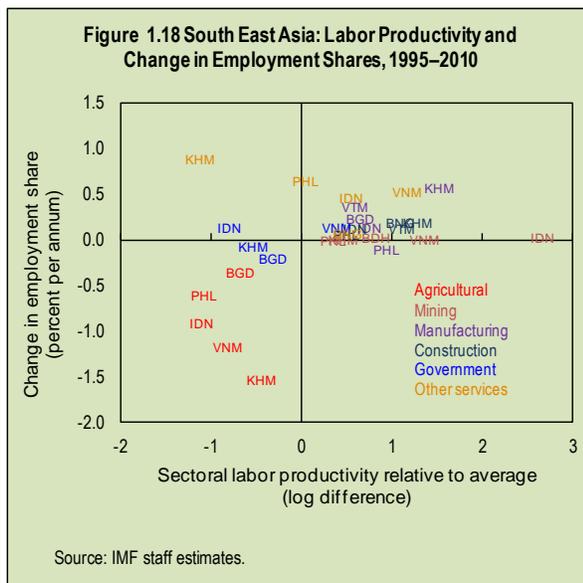
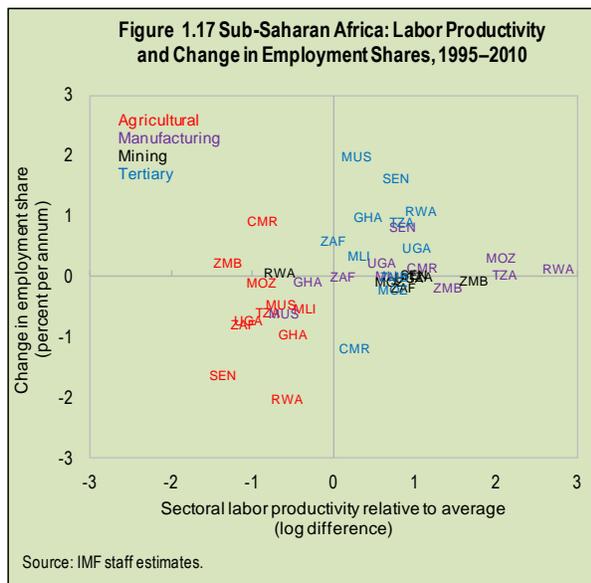
Figure 1.16 compares a sample of SSA countries (Cameroon, Ghana, Mauritius, South Africa, and Tanzania) with a group of low- and middle-income Asian economies that have experienced rapid structural transformation and started their growth takeoffs with similar or lower levels of GDP per capita than the average SSA country at the time. As can be seen, Ghana and Tanzania have experienced declines in agricultural output and employment shares over time, with Tanzania matching the experience of the comparator Asian economies quite closely. The middle-income countries have experienced declining manufacturing ratios for the past two decades, consistent with the process in more advanced Asian countries, where services play an ever-increasing role in the economy. Relatively few LICs in SSA (Mozambique, Tanzania) have been able to raise their manufacturing output and employment shares on a sustained basis.

**Figure 1.16. Sub-Saharan Africa: Sectoral Output and Employment, 1995–2010**



Sources: CEIC database; Haver Analytics database.

An alternative presentation of the data on employment shares shows broad increases in employment in sectors with higher productivity. Figures 1.17 and 1.18 depict annual changes in employment shares against average relative productivity levels for agriculture, manufacturing, mining, and the tertiary sector for SSA and Asian countries, respectively.<sup>23</sup> Points in the lower left quadrant indicate sectors with below average productivity and declining employment shares, while those in the upper right quadrant indicate sectors with above average productivity and rising employment shares.



To the extent that the observations for manufacturing and services in most countries are located in the upper right quadrant, corresponding to movements from low to high average labor productivity sectors, it shows that there has been structural transformation. In fact, only Cameroon and Zambia show change in the employment share in the opposite direction, namely, from high to low average labor productivity sectors. In all the other SSA countries, workers have moved out of the agricultural sector (in red). This suggests that the findings of McMillan and Rodrik (2011), whose analysis of a smaller subset of countries through 2005 found workers moving into low-productivity sectors, may actually be reversed when considering a broader set of countries through 2010.

There are important differences across country groups within SSA. Most oil exporters, middle-income and non-fragile low-income countries have seen sustained increases in average labor productivity, often underpinned by rising productivity in agriculture and resulting in a declining share of GDP from that sector. Fragile countries, in contrast, have generally experienced low and irregular growth, largely as a result of conflict; this poor growth is reflected in the absence of significant structural transformation in most of these countries.

<sup>23</sup> The initials appearing in the graphs correspond to the following countries: Cameroon (CMR), Ghana (GHA), Guinea (GIN), Mali (MLI), Mauritius (MUS), Mozambique (MOZ), Namibia (NAM), Rwanda (RWA), Senegal (SEN), South Africa (ZAF), Tanzania (TZA), Uganda (UGA), Zambia (ZMB); Bangladesh (BGD), Cambodia (KHM), Indonesia (IDN), Philippines (PHL), and Vietnam (VNM) .

The fact that most countries in SSA that have been growing faster than in the past have not experienced an increase in the share of manufacturing in employment or GDP, in contrast to the experience in Asia, is not necessarily surprising. To some extent, this pattern is what would be expected given the differences between the two regions in resource endowments and in comparative advantage: when Asia started its take-off, most countries were abundant in labor, while SSA is abundant in natural resources. The challenge is that many of those natural resource sectors, such as mining, are capital intensive, and will not provide the jobs needed to accommodate the rapidly growing working age populations in the region.

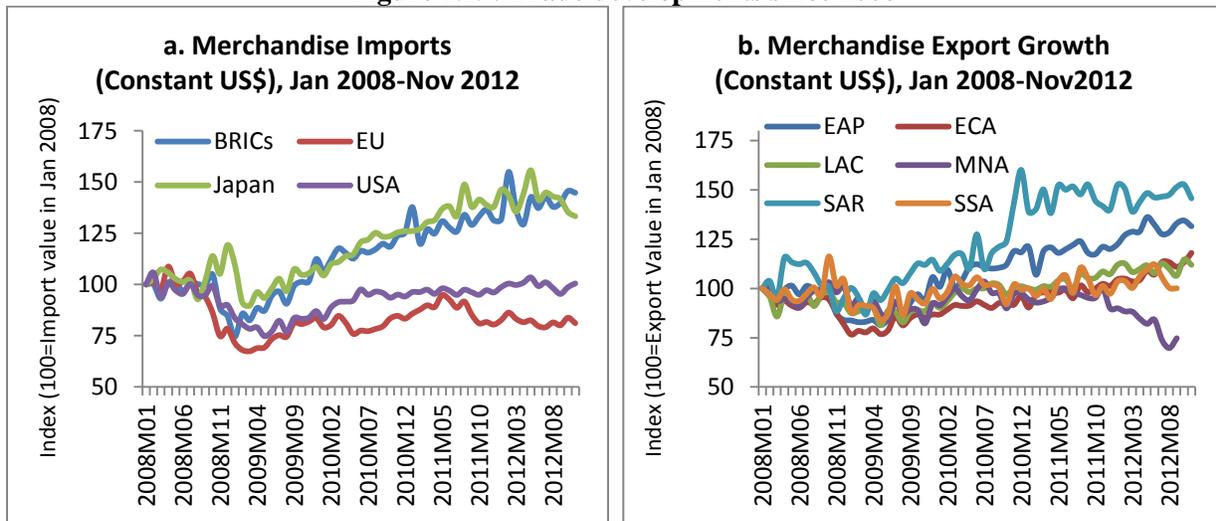
The recent growth in real wage levels in China, together with SSA's demographic dividend—implying declining dependency ratios in the future—suggest that manufacturing in SSA could become increasingly competitive. But irrespective of whether economies grow through strengthening the manufacturing sector (Tanzania, Mozambique) or services (Kenya, Mauritius), it is unlikely that they can do so without first experiencing a major acceleration of agricultural productivity growth.

## **Update on trade trends and trade policy developments**

### **Post-crisis recovery in trade has been uneven**

Since the outbreak of the financial crisis over four years ago, global interdependency has been underscored by the largely synchronized nature of trade trends between high income and developing countries. As of November 2012, neither the U.S. nor the EU had surpassed pre-crisis levels of imports, although their combined share of world imports remains sizeable, at roughly one-quarter of the total. On the other hand, Japan and large emerging economies like Brazil, Russia, India, China, and South Africa (the BRICS) have seen their import levels rise steadily above pre-crisis levels, a trend that began in early 2009 (Figure 1.19). These divergent recovery trends have translated into weak trade performance in regions that have traditionally relied on U.S. and EU markets. Exports from Europe and Central Asia (ECA), Latin America and the Caribbean (LAC), and Sub-Saharan Africa (SSA) all hover only slightly above pre-crisis levels. The situation is especially dire for non-GCC countries in the Middle East and North Africa (MENA), where political developments combined with external economic factors have led to a steady decline in exports since late 2011. Meanwhile, other regions have adjusted with more success. The East Asia and Pacific (EAP) region has experienced steady positive real export growth, fueled not only by China, but also by smaller economies such as Cambodia, Vietnam, Thailand, and Lao PDR. In South Asia (SAR), positive real export growth in India and Bangladesh helped the region experience the strongest export recovery, peaking in December 2010 at a level one and a half times higher than pre-crisis levels. Since then, however, SAR's export performance has been lackluster.

**Figure 1.19: Trade developments since 2008**



Source: World Bank Datastream.

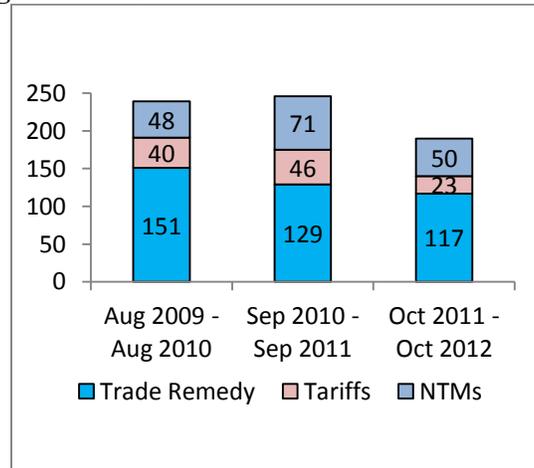
Source: World Bank Datastream.

Global trade in 2012 was hampered by a mid-year slump in global imports and steadily contracting import demand on the part of high income countries, with the Euro area at the epicenter. Growth rates for world imports of industrial goods during the first half of 2012, year-over-year, were negative (World Bank 2013). At the same time, increased import demand in developing countries helped mitigate the dearth of demand in high income economies. Developing countries' real exports also fluctuated considerably in 2012, with differences across countries and regions.

### Protectionist outbreak avoided despite uncertain future for global economy

According to World Trade Organization's (WTO) monitoring of trade protectionist measures, 190 new trade-restrictive measures were introduced by G20 countries between mid-October 2011 and mid-October 2012 (see Figure 1.20). While this represents a slowdown compared with previous years, the new measures add to the stock of restrictions put in place since the outbreak of the crisis. The growing accumulation of trade restrictions is of concern not only because it undermines the benefits of trade openness, but it also exacerbates the combined effects of the new measures with pre-crisis restrictions and distortions, such as agriculture subsidies and tariff peaks. Nevertheless, in the five months leading up to October 2012, the pace of removal of previous measures was better than in previous periods (21 percent overall have been removed since October 2008).

**Figure 1.20: G20's new trade restrictive measures**



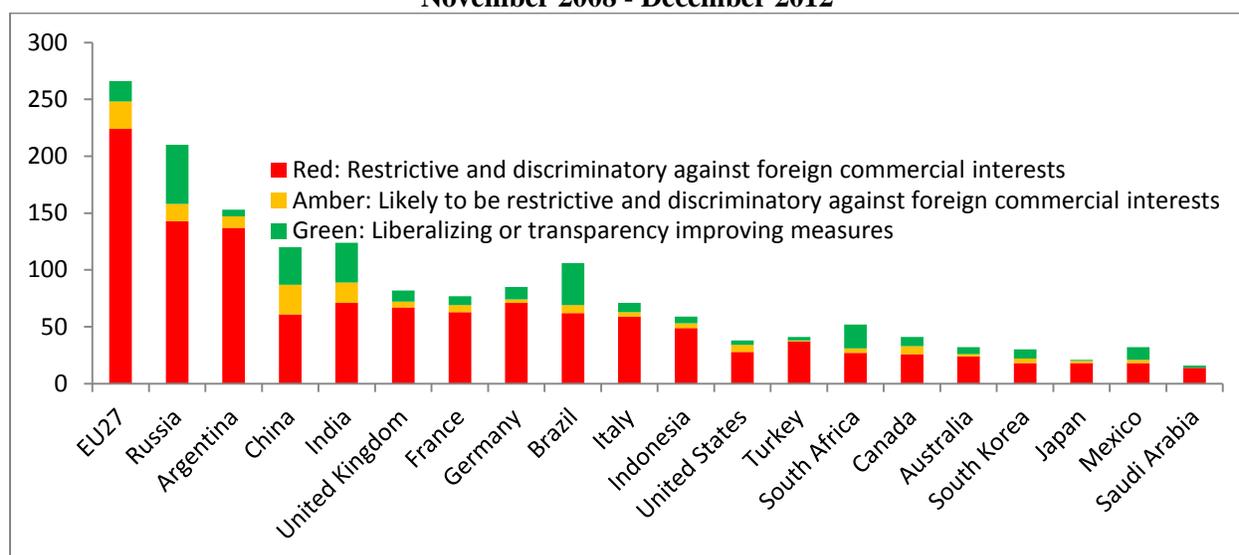
*Note: Different methods of codification may lead to small discrepancies between these and other tallies of trade-restrictive measures*

*Source: World Trade Organization.*

G20 countries, which have repeatedly committed to refrain from adopting trade-restrictive measures, now account for an increasing share of those measures: 74 percent in 2012, up from 60 percent in 2009 according to the Global Trade Alert (GTA),<sup>24</sup> which provides broader coverage than the WTO in terms of both countries and policy measures included in the database. India, the EU, Argentina, Brazil, and Russia are among the countries that have implemented the highest number. Globally, the most frequently used trade-restrictive measures are state aids and anti-dumping, followed by import tariff increases and non-tariff measures. Initially, restrictive measures were seen as policy responses to mitigate the temporary effects of the global financial crisis. However, recent measures appear to be more embedded in national industrial plans, and hence longer term in nature (World Bank 2013). G20 countries are simultaneously responsible for a majority (66 percent) of all trade liberalizing measures. However, trade liberalizing measures represent only a quarter of all measures enacted to date (Figure 1.21).

<sup>24</sup> [www.globaltradealert.org](http://www.globaltradealert.org)

**Figure 1.21: Total number of measures implemented and still in force by each G20 country November 2008 - December 2012**



*Note:* Individual measures may cover a very large portion of trade or just one product—these data are therefore not necessarily reflective of trade coverage. For example, Mexico reduced tariffs on 5,000 tariff lines, but this is reflected in just a few “measures.”

*Source:* Global Trade Alert database.

### Limited progress in Doha Round negotiations at the WTO

The need for multilateral agreement remains critical to mitigate the use of trade restrictive measures and promote trade openness. However, the prospects for successfully concluding the Doha Development Agenda (DDA) negotiations—now entering their twelfth year—remain dim, with recent reports that WTO members have turned their attention in 2013 to “realistic” deliverables<sup>25</sup>, rather than a conclusion to the whole round. The deadlock is costly. In terms of the market access dimension of what has been negotiated to date, there is a potential global welfare boost of some US\$160 billion at stake (Hoekman 2011). But often overlooked is the opportunity cost of the WTO not being able to deliver on its “legislative” function as an arbiter of new rules of the game in policy matters outside the framework of the DDA. These include “green” industrial policy measures, natural resource- and climate-related trade policies (e.g., carbon border adjustments), and export restrictions on food products to insulate domestic markets. DDA paralysis carries the risk of countries pursuing unilateral, potentially damaging, responses to the externalities of these policies.

According to experts, much could be gained if a critical mass of the 15-20 or so largest WTO members were to agree to reduce applied barriers to trade and bind current levels of openness, but currently some large countries want more than other large countries are willing to offer (Hoekman 2011). Over the course of 2012, topics including trade facilitation, agriculture, special and differential treatment, least developed country (LDC) issues, and dispute settlement were advanced—according to the chairs of the various Doha negotiating groups—while others, like services, barely moved at all, and are unlikely to move forward in the months ahead. Successful negotiations at the upcoming December 2013 ninth ministerial conference in Bali are being viewed as a pivotal stepping stone—and necessary precondition—for ending the Doha

<sup>25</sup> The realistic deliverables refer to the topics in which negotiations saw progress over the past 12 months, including trade facilitation, agriculture, special and differential (S&DT) treatment, LDC issues, and dispute settlement.

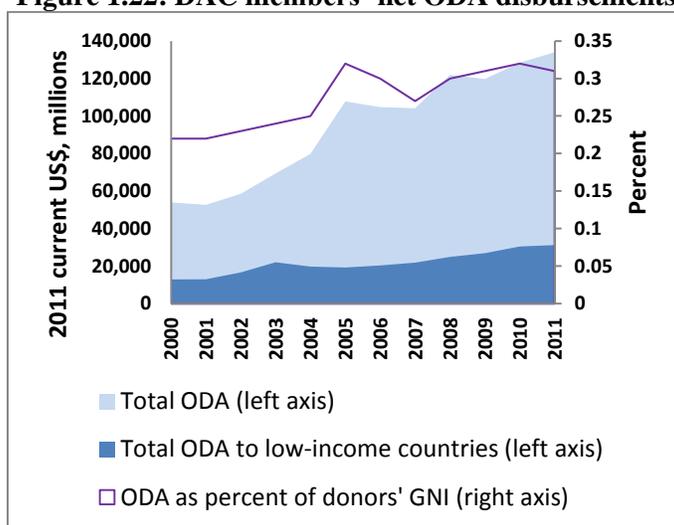
Round, though there is little optimism that the conference itself will end the round (ICTSD 2012). At the most recent World Economic Forum in Davos, trade ministers from over 20 WTO member countries gathered informally and imposed an unofficial Easter deadline for taking stock of whether “meaningful results” in Bali will be possible. They agreed that success at the conference would have to include gains in the areas of trade facilitation, LDC issues, and agriculture (ICTSD 2013).

## Aid and international financial institutions

### Recent trends and prospects of aid

Over the last decade, official development assistance (ODA) steadily increased, reaching its peak in 2010. The general trend of rising annual flows during the 2000s only slowed after the global financial crisis in 2008, with a deceleration in growth of 1 percent in 2009. ODA continued to be a stable source of development financing even after the global financial crisis, helping to alleviate the immediate impact of previous financial crises. However, in 2011, as the effects of the recession hit donors’ aid budgets, the recipients of ODA suffered the first year of lower aid disbursements since 1997 (excluding fluctuations affected by exceptional debt relief).

**Figure 1.22: DAC members’ net ODA disbursements**



Source: OECD DAC and World Bank.

### Bilateral and Multilateral Aid

DAC members disbursed US\$125.5 billion (in constant dollars) in 2011, compared to US\$128.4 billion the previous year, a decrease in real terms of 2.3 percent. In current prices ODA equaled to US\$134 billion, up from US\$128 billion in 2010. As a percentage of donors’ combined gross national income (GNI), ODA went from 0.32 percent in 2010 to 0.31 percent in 2011 (see Figure 1.22). The current situation represents some concern, since developing countries have also been hit by the effect of the crisis. Within total net ODA, the bilateral share of net ODA decreased somewhat from 71 percent in 2010 to 70 percent in 2011, indicating a small increase in the share of multilateral aid to close to 30 percent. One of the broad trends in the recent international aid architecture is the rapid increase of “multi-bilateral” ODA, which is defined as bilateral ODA earmarked for a specific purpose and channeled through the multilateral system. According to OECD DAC, multi-bilateral ODA has increased from \$ 9 billion to \$

16.7 billion between 2007 and 2010, representing 12 percent of gross ODA excluding debt relief. The World Bank channels over a quarter of such multi-bilateral ODA, becoming the single largest multilateral channel for trust funds.

## Gleneagles

At the Group of Eight Gleneagles summit in 2005, important commitments related to ODA and external debt forgiveness were made. Indeed, the international agreement on debt relief (Multilateral Debt Relief Initiative, or MDRI) cancelled US\$56.5 billion in loans owed to the World Bank, the African Development Bank, and the International Monetary Fund (IMF). In addition, DAC donors agreed to increase ODA by US\$50 billion between 2004 and 2010, at least half of which would be designated for Africa, i.e., SSA and North Africa. This promised increase of US\$50 billion was made in 2004 prices and exchange rates, such that the targeted level of ODA in 2010 prices was estimated to be US\$152.2 billion. Given the actual amount of US\$128.5 billion available, a gap of over US\$25 billion still remains. The OECD DAC's 2012 annual ODA report shows that only a little over US\$1.2 billion of the shortfall can be attributed to lower than expected GNI levels due to the economic crisis (OECD 2012a).

At Gleneagles, the G8 donors also envisaged a raise in total ODA to Africa of US\$25 billion in 2004 prices and exchange rates. In current prices and exchange rates, this translates into an increase of an estimated US\$29 billion and US\$31 billion in 2010 and 2011, respectively. Yet estimates show that Africa only received an additional US\$11.8 billion in 2010.

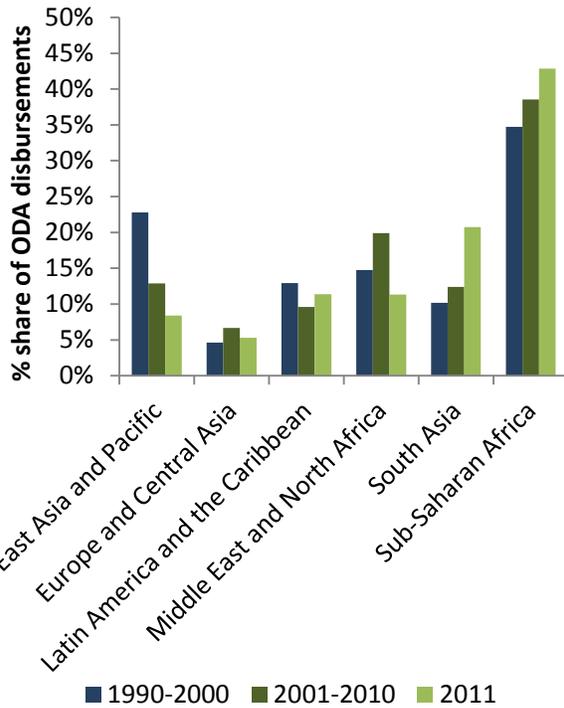
## Regional aid

Although ODA disbursements were lower in 2011, the trend in regional ODA remained stable compared to the previous year. Aid is mainly concentrated in SSA, which received 43 percent of net ODA disbursements in 2011, and in South Asia (21 percent) and MENA (11 percent) (Figure 1.24).

While **Sub-Saharan Africa** still received most of the aid, this region suffered a decrease in 2011, with flows of US\$24.3 billion. This amount represents a fall of 0.6 percent in real terms compared to 2010. **Europe and Central Asia** also saw a fall in net bilateral ODA flows of 17 percent in real terms from 2010; between 2010 and 2011, the decline was around 6 percent as the region has made strong gains toward poverty alleviation. **Latin America** suffered a decrease of 3 percent in 2011, while South Asia registered a shortfall of 2 percent. The only region with an increase in net ODA disbursements was the **Middle East and North Africa**, as the revolutions in this region triggered more aid.

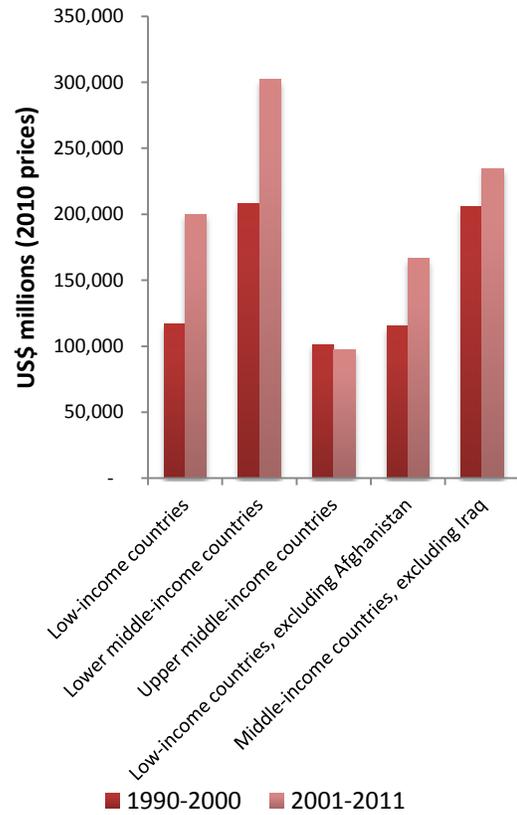
Low income countries also received 3 percent more aid compared to 2010. Middle income countries, on the other hand, suffered a decline of 17.2 percent from 2010. For lower middle income countries, net ODA disbursements decreased 8.87 percent from 2010, at US\$5.7 billion (Figure 1.23).

**Figure 1.23: Net ODA disbursements to developing regions**



Source: OECD DAC 2012.

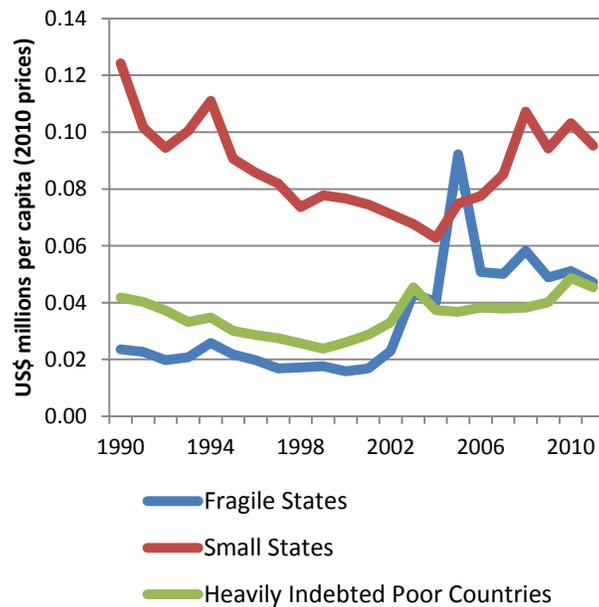
**Figure 1.24: Net ODA disbursements to low- and middle-income countries**



## Special groups

Fragile, small, and heavily indebted poor countries also suffered the consequences of a smaller amount of ODA disbursements from 2010 to 2011 (Figure 1.25). **Fragile States (FCS)** received 6 percent less ODA disbursements than in 2010; **Small States (SST)** also received six percent less than in 2010; and the flow to **Heavily Indebted Poor Countries (HIPC)** decreased by 4.1 percent.

**Figure 1.25: Net ODA disbursements to fragile, small, and HIPC states**



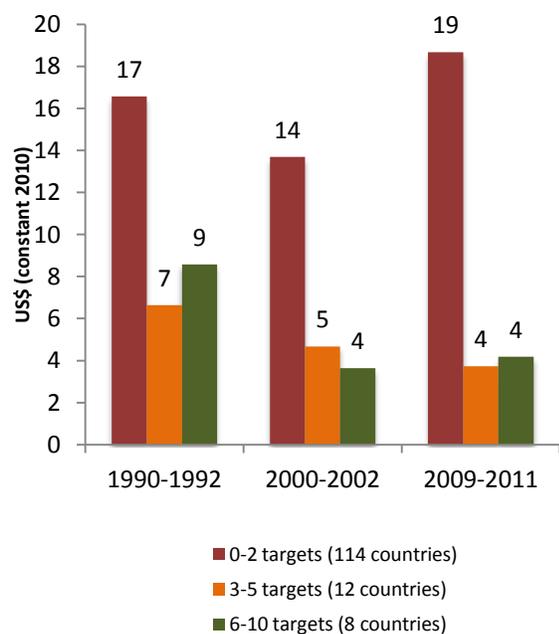
Source: OECD DAC 2012.

Fragile states are the developing countries most challenged in meeting the Millennium Development Goals. They are typically characterized by weak institutions and macroeconomic instability. The countries often find themselves in internal conflict or with severe political instability. For obvious reasons peace- or state-building activities take priority over economic policymaking. Macroeconomic policy advice and implementation are hampered by lack of timely and reliable statistics. International organizations' and development partners' effective engagement requires recognizing fragile states' limited capacity and large financing needs.

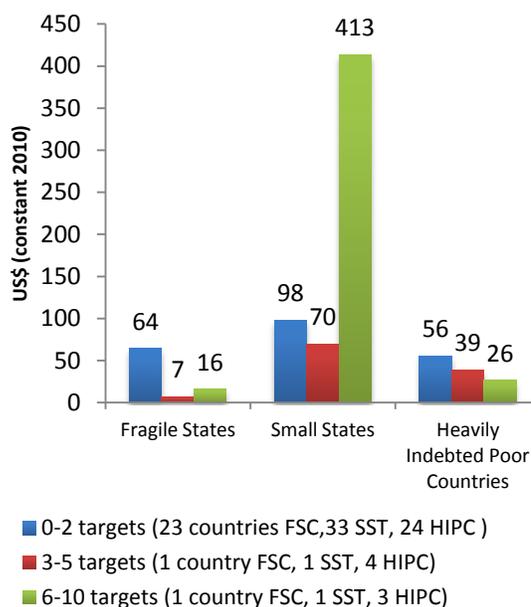
Fragile states are vulnerable countries with few if any resources available with which to address vulnerabilities. In a possible protracted slowdown of global growth these countries would be hard pressed to counteract the accompanying negative shocks on their economies, either by depleting available policy buffers or adjustment of macro policies. With domestic policy space severely limited, these countries would have to turn to the international community for additional assistance if such a downside risk scenario were to materialize. Therefore, the decline in ODA for these countries is extra worrisome as well-targeted external financial aid can be effective in supporting countries exiting from fragile situations (World Bank 2011).

Even though aid fell in 2011, the flows are still being directed to those countries lagging the most (i.e., the countries furthest from achieving the MDGs). For example, the group of countries in a fragile situation that have met or are currently on track to achieve no more than two MDGs received an annual average of US\$64 per capita in 2009-11 (Figure 1.26). Even if all developing countries are considered, ODA disbursements per capita have increased for countries with no more than two of the MDGs achieved (Figure 1.27).

**Figure 1.26: Net ODA received per capita by groups of countries ranked by MDG targets met or on track to be met by 2015**



**Figure 1.27: Net ODA received per capita by groups of countries ranked by MDG targets met or on track to be met by 2015 (2009-2011)**



Source: OECD DAC 2012.

## BRICS

ODA DAC resources are not the only resources that countries can use to attain the MDGs, and various new donors and philanthropists have become part of the development community, providing resources to countries to make progress towards the MDGs and to development in general. In particular, South-South cooperation has become increasingly important, with estimates of financial aid flows from the so-called BRICS to developing countries of up to US\$4 billion in 2009 (Adugna *et al.* 2011). However, aid volumes do not fully capture the significance and impact of BRICS on the financial inflows of low-income countries. For example, since 2000, trade between BRICS and Sub-Saharan Africa has increased 25 percent annually, reaching USD206 billion in 2011.

Trade, foreign direct investment, and development aid are often intertwined and come as a package based on the idea of South-South cooperation, which is based on solidarity, shared experiences, and self-reliance of the South (Yamoussoukro 2008). Even though foreign assistance is diverse among BRICS, development cooperation: (i) focuses on trade partners, and consequently, often on neighboring countries and regional integration, to stimulate trade, investments, and growth as the main vehicles for

improvement in development outcomes; and (ii) focuses aid on technical rather than financial assistance (EU 2012).

### Looking forward: ODA flows through 2015

Looking beyond 2011, for the ODA flow to developing countries to remain constant in per capita terms, an increase in total ODA by 2015 of US\$7 billion in 2011 prices and exchange rate is needed. Given the ongoing fragility of the economic recovery in most of the developed world, this might be quite a difficult undertaking to accomplish at a time when any additional assistance to facilitate the attainment of the MDGs could prove critical. Continuing at the current level of ODA would result in a fall of 1.2 percent annually until 2015.

Country programmable aid (CPA) is a core subset of ODA, and represents about 67 percent of total DAC ODA, with 95 percent of multilateral agencies and 45 percent of bilateral aid agencies reporting on their programmable aid flows. CPA data provide information about the forward spending plans by DAC donors on development.<sup>26</sup> CPA is a reliable predictor of actual disbursements, with predictability ratios of 103, 95, and 92 percent in 2009, 2010, and 2011, respectively. A ratio of 92 percent means that, on average, donors disbursed 8 percent less than planned the year before.

The 2012 DAC report on predictability presents the results of the 2012 DAC survey on forward spending plans for 2012 to 2015, the final year by which the current set of MDGs should be achieved. The survey data indicate that the annual amount of CPA in 2012 is anticipated: to jump by 6 percent in real terms compared to 2011; to remain constant in 2013 compared to 2012; and to fall by 1.5 percent in 2014 and by another 1 percent in 2015. This results in a slight decline in per capita CPA from US\$16.3 to US\$16.2 in 2015 (in 2011 prices and exchange rates). The implications of this decline are more pronounced in SSA, which received US\$38.5 per capita CPA in 2011 and will see its allocation decline to US\$36.2 per capita by 2015. Although the initial recovery bodes well for the availability of ODA to assist with the attainment of the MDGs, the downturn in the outer years does not.

### Aid effectiveness

Since the Fourth High Level Forum on Aid Effectiveness at Busan (HLF4), Korea, in late 2011, the international community has shifted from aid effectiveness to a broader focus on effective development cooperation. Though the aid effectiveness agenda remains important, this shift reflects a recent evolution of the development landscape which includes:

- Support for country-led management of development support with a focus on results, in lieu of the traditional discussion focused on donor harmonization and alignment.
- The expanding role of new development partners, such as middle-income countries, the private sector, and civil society organizations, in development.
- The growing importance of aid as a resource for catalytic change and institutional development.

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<sup>26</sup> CPA is total ODA corrected for aid that is inherently unpredictable (humanitarian and disaster relief aid), entails no flows to the recipient country (such as donor administrative cost), and its use is determined through dialogue between the donor agency and partner government. In addition, loan repayments are netted out as those that are not normally part of aid allocation decisions by donor governments (OECD 2010)

- The changing global financial base for development, with private financing playing a growing developmental role.
- The emergence of new technologies to increase global connectivity and transparency and accountability.

The *Busan Partnership for Effective Development Co-operation* calls for the establishment of a “new, inclusive, and representative Global Partnership for Effective Development Co-operation to support and ensure accountability for the implementation of commitments at the political level.” At the most recent meeting of the Working Party on Aid Effectiveness (WP-EFF) in June, 2012, the WP-EFF (which has led the aid effectiveness agenda at the global level since the Paris Declaration on Aid Effectiveness in 2005) formally agreed to establish the Global Partnership for Development Cooperation. The Global Partnership consists of three co-chairs and 18 steering committee members and has been operational since late 2012. The World Bank is one of the steering committee members representing the Multilateral Development Banks (MDBs) (see Box 1.1 on operationalizing the Busan Partnership).

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### **Box 1.1: Operationalizing the Busan Partnership for Effective Development Co-operation**

During the HLF4, the international community made a renewed commitment to moving the effective development cooperation agenda forward while keeping its focus on the unfinished aid effectiveness agenda. Three key vehicles used to bring these agendas forward are: (i) the Global Partnership for Effective Development Cooperation; (ii) the Global Monitoring Mechanism; and (iii) Building Blocks for Post-Busan Implementation.

To discuss the direction of the post-Busan Effective Development Cooperation Agenda, the international community established the Post-Busan Interim Group (PBIG) - an interim discussion platform. The PBIG held several meetings in the first half of 2012 and agreed on the Global Partnership mandate and the global monitoring framework. The Global Partnership mandate focuses on: (i) maintaining and strengthening political momentum for more effective development co-operation; (ii) ensuring accountability for implementing Busan commitments; (iii) facilitating knowledge exchange and sharing lessons learned; and (iv) supporting implementation of the Busan commitments at country level.

The indicators and associated targets of the global monitoring framework (successor of the 2005-2010 Paris Declaration Monitoring Survey) intend to promote international accountability for implementing the Busan Partnership agreement. Five out of 10 indicators are from the Paris Declaration Monitoring Survey (e.g., use of country PFM and procurement systems) which ensures continuity with the unfinished aid effectiveness agenda. The remaining five indicators are new and reflect the evolution of the development landscape by including civil society and private sector engagement. The Building Blocks launched at the HLF4 are initiatives to help further progress in eight key areas, including: (i) conflict and fragility; (ii) South-South cooperation; (iii) private sector; (iv) climate finance; (v) transparency; (vi) effective institutions and policies; (vii) results and mutual accountability; and (viii) managing diversity and reducing fragmentation.

To date, three minister level co-chairs and 18 steering committee members have been appointed from partner countries, development partners, the private sector and CSOs. The first steering committee meeting to discuss focus areas of the Global Partnership was held in December 2012. The global monitoring framework is being finalized. Given their voluntary nature, the progress of the Building Blocks varies across initiatives. Going forward, a key challenge for the Global Partnership is to connect with other international fora and initiatives, most notably the discussion on the post-2015 MDG goals.

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Until the Fourth High Level Forum meeting on Aid Effectiveness in Busan in 2011, the BRICS saw themselves primarily as recipients of aid. In Busan, an agreement was reached to fold the Working Party on Aid Effectiveness into a new Global Partnership for Effective Development Cooperation,<sup>27</sup> which held its first meeting in June 2012. The new Global Partnership brings together developing countries, including major providers of South-South cooperation such as the BRICS, donor countries, civil society organizations, and private funders. It is expected that the Global Partnership will represent a window of opportunity for a balanced international dialogue among all development partners, including traditional DAC donors and non-DAC donors such as the BRICS. To date, over 160 countries and 45 organizations from around the world have endorsed the Partnership.

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<sup>27</sup> The Global Partnership is a forum for knowledge exchange and regular monitoring of progress. The main functions will be to: maintain and strengthen political support for more effective development co-operation; carry out monitoring of the implementation of the Busan commitments; facilitate knowledge exchange and lesson learning; and support the implementation of the Busan commitments at the country level (<http://www.aideffectiveness.org/busanhlf4/about/global-partnership.html>).

Notwithstanding the upcoming changes that will potentially emerge from the new Global Partnership, it is important to continue to monitor promised progress by the DAC donor community as a means to improve aid effectiveness as set forth in the Paris Declaration on Aid Effectiveness. This remains valid, particularly given the need to improve effectiveness of ongoing aid programs such that additional progress towards the MDGs can be achieved.

The Paris Declaration on Aid Effectiveness, which placed country ownership of policies and programs at the center of a reform agenda to make aid more effective, committed donors and developing countries to be mutually accountable for implementing the declaration through a set of 13 measurable targets (World Bank 2012; OECD 2012b). By the 2010 deadline, only one of the targets had been met: to strengthen capacity by coordinated support (target 4).

However, disaggregating the data for the various multilateral development banks and other international organizations such as the United Nations, and the EU institutions, yields a more nuanced picture (Table 1.7). For example, the Inter-American Development Bank has met four out of the eight indicators for which disaggregated data exist, the World Bank three (see Box 1.2 for additional information about World Bank performance in development cooperation), and the EU institutions two. All other multilateral development banks have met one indicator.

Table 1.7 also shows that in many areas, progress has been made by individual international organizations, but each of them has also fallen back on at least one target. The African Development Bank and the Asian Development Bank show deteriorations in four of the eight indicators analyzed. The World Bank (see Box 1.2) is closest to reaching all indicators, with an average gap of 17 percent remaining on seven of its on-met indicators, while the Inter-American Development Bank has an average remaining gap of well over 60 percent on its remaining four indicators. The UN also remains significantly far from reaching its remaining targets, as it was only halfway there in 2010.

## **Box 1.2: World Bank Performance on Development Cooperation**

The World Bank's performance on development cooperation has continuously improved and is amongst the strongest of all development partners. Evidence from international assessments, including the Paris Declaration Survey, confirms the Bank's sustained commitment to improve its own effectiveness in support of stronger development outcomes. With the Global Partnership for Effective Development Cooperation in mind, the Bank focuses on the following priorities:

***Partner Country Leadership and Ownership.*** The Bank promotes better development cooperation and more effective institutions by:

- Aligning its support with each country's development priorities.
- Focusing on capacity development, investing in human capital, and strengthening stakeholder ownership to facilitate achievement of national development goals.
- Supporting public sector institutions and systems through better diagnostic, analytical, and measurement tools.
- Enabling stronger government-led management of development support and greater integration of aid and other support into national budgets.
- Strengthening and using country systems—for budget and project management, procurement, financial management, environmental and social safeguards, and results measurement—with the ultimate objective of transforming development support into sustainable results.

***Results.*** The Bank adopts results-orientation implementation by:

- Implementing a Corporate Scorecard, an institutional-level IDA Results Measurement System, and an Annual Results Report.
- Mainstreaming a results culture with systematic results frameworks for all lending projects, programs, and country assistance strategies, as well as the adoption of new results-oriented financing instruments such as the Program for Results (P4R); and increasing impact evaluations and evidence based decision making through the collaborative Bank/partner country Development Impact Evaluation Initiative (DIME).
- Supporting country capacity to implement results-based approaches; building country statistical capacity to support enhanced and rigorous monitoring and evaluation; and working with regional Communities of Practice for cross-country knowledge exchange and capacity development on results management.
- Using innovative tools such as geo-mapping, beneficiary feedback, third party monitoring, and other mechanisms to enhance social accountability and improve service delivery.

***Transparency.*** The Bank has made great strides in the area of transparency by:

- Launching an Access to Information Policy, the Open Data and Open Knowledge initiatives, and the Open Access Repository. These initiatives encourage public access, help improve accountability, and link funding to development outcomes and results.
- The Aid Transparency Index from Publish What You Fund, and the transparency component of the Center for Global Development's QuODA assessment both identify the Bank as a global leader on transparency.
- Demonstrating leadership as an active proponent and implementer of the International Aid Transparency Initiative (IATI), which sets a common standard for all development partners to share aid data.
- Supporting recipient country Open Government initiatives and efforts to improve budget management and transparency for domestic accountability.
- Promoting aid predictability to facilitate greater transparency.

- 
- AidFlows (<http://www.aidflows.org/>) is a publicly available web based source of information about aid flows and seeks to better inform the global conversation about development funding. AidFlows began as a partnership between the OECD-DAC and the World Bank. AidFlows provides easy access to the by-country information in an intuitive visual format. The site has been very well received by a range of users, including government officials in donor and recipient countries, aid agencies, MDBs, NGOs, and civil society

***Development Partnerships Beyond Aid.*** The Bank integrates key themes and opportunities presented by the evolving development landscape through:

- Partnering with lower- and middle-income developing countries to facilitate support through South-South cooperation, including knowledge exchanges, technology transfers, investment, trade, and financial support.
- Leveraging funding from middle-income countries, the private sector, foundations, global funds and programs, and other sources that contribute significantly to development.

Countries in fragile and conflict situations face complex development challenges and are a special area of focus for the Bank. The *New Deal for Engagement in Fragile States* sets out a collective vision and principles for engagement with these fragile and conflict-affected countries. The Bank is spearheading efforts in several key areas critical to successfully implementing the New Deal, such as supporting technical capacity in the G7+, piloting Peace-building and State-building Indicators for partner countries, and actively supporting forums for strengthening partnership among partner countries, donors, MDBs, civil society organizations, and the private sector.

Recognizing that progress on development cooperation at the global, institutional, and country levels is interlinked, the World Bank: continues its engagement and leadership in international platforms, initiatives, and partnerships; leads and innovates through institutional reforms, policies, and practices; and promotes support for country-led and –owned development efforts.

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**Table 1.7: Progress on Paris Declaration survey indicators by multilateral development banks, UN, and EU institutions**

Global Target	Overall Result	MDB Performance			World Bank			African Development Bank			Asian Development Bank			Inter American Development Bank			United Nations			EU Institutions		
		%	2010 (%)	Progress since 2005	2010 (%)	Gap	Progress since 2005	2010 (%)	Gap	Progress since 2005	2010 (%)	Gap	Progress since 2005	2010 (%)	Gap	Progress since 2005	2010 (%)	Gap	Progress since 2005	2010 (%)	Gap	Progress since 2005
3- Aid flows are aligned with national priorities	85	72	36	=	79	7%	+	59	31%	+	64	25%	-	48	44%	+	31	64%	-	51	40%	+
4 - Strengthen capacity by coordinating support	50	58	50	+	73	Met	+	69	Met	+	44	12%	+	65	Met	+	67	Met	+	50	Met	+
5 - How much aid for the government sectors uses country systems	55	35	20	+	55	Met	+	32	42%	-	29	47%	-	5	91%	+	12	78%	+	47	15%	+
6- Strengthen capacity by avoiding parallel PIUs	-67	-32	-49	+	-80	Met	+	-65	3%	+	-95	Met	+	-7	90%	=	1	102%	-	-71	Met	+
7 - Aid is more predictable	71	43	29	-	51	28%	-	50	30%	+	54	24%	-	48	32%	-	23	68%	+	48	32%	+
9 - Use of common arrangements or procedures	66	45	32	+	59	11%	+	35	47%	-	50	24%	+	80	Met	-	45	32%	+	52	21%	+
10a Joint Missions	40	19	18	+	29	28%	+	14	65%	-	15	63%	+	67	Met	+	38	5%	+	19	53%	-
10b - joint country analytical work	66	43	32	=	59	11%	+	50	24%	-	39	41%	-	75	Met	+	61	8%	=	57	14%	+

Source: OECD DAC 2012.

## Acceleration towards the MDGs

Various other mechanisms exist to accelerate progress towards the MDGs in addition to improvements in aid effectiveness. For example, in 2010, the United Nations Development Programme (UNDP) developed an MDG acceleration framework (MAF) to provide a systematic way of identifying bottlenecks and possible high-impact solutions that could assist countries to pick up the pace towards the attainment of the MDGs. The framework was rolled out in ten countries across a range of MDGs in 2010, and has been used since then to assist 44 countries across almost all of the MDGs. This has led to concrete plans of action with coordinated roles for governments and all development partners involved in achieving countries' MDG priorities.

The results from the MAFs completed to date are encouraging and have led to increased collaboration between the World Bank and the UN in this area. The initial lessons learned include the importance of strong national ownership, facilitation of cross-sectoral collaboration, and CSO and NGO participation. For the countries themselves, of critical importance is actual implementation of the agreed-upon MDG action plan, which includes ensuring that gaps in institutional capacity and sector governance are addressed, that the MDG action plan is adequately incorporated into annual or multi-year partner support plans, and that both intermediate and final indicators of MDG achievement are regularly monitored, all to ensure that efforts are yielding the desired results.

## Improving the effectiveness of projects through the use of ICT

The use of information and communications technology (ICT) for economic development was recognized at the time of the adoption of the official list of MDG indicators as part of MDG 8, which focuses on the deepening of a global partnership for development. A specific description of this sub-MDG was chosen and indicators identified. Target 8F states that in cooperation with the private sector, the benefits of new technologies, especially those related to information and communications, will be made available.

An evaluation of these indicators shows that mobile phone subscriptions have risen spectacularly across the globe, while growth in the number of fixed telephone lines has stagnated. Impressive increases have also taken place in internet usage, although here progress is more diverse, with stronger growth in high income countries than in low and middle income countries. Even though access challenges remain, particularly in low income countries, the spectacular rise in mobile phone penetration has allowed for a variety of innovations to emerge that allow citizens, governments, and international organizations to be more engaged and better informed, and that enable aid programs to identify and communicate more directly with beneficiaries.

In addition to the various business opportunities that have emerged due to the evolution of ICT, a range of opportunities to improve the effectiveness of government programs and associated aid financing, consequently accelerating attainment of the MDGs, has been brought about in parallel. Table 1.8 illustrates how mobile telephone technology has assisted countries in making progress towards each MDG. Many more current examples demonstrate how ICT can facilitate service delivery. Indeed many governments around the globe, in varying stages of development, are adopting ICT, particularly mobile technologies, to assist in this endeavor. At the same time, various international aid agencies are exploring

opportunities to deliver aid more effectively using ICT (e.g., Swiss Agency for Development and Cooperation 2011).

**Table 1.8: Mobile technology and the Millennium Development Goals**

MDG	Example
<p><b>Poverty and hunger</b></p> 	<p>A study on grain traders in Niger found that cell phones improved consumer welfare (Aker 2008). Access to cell phones allowed traders to obtain better information about grain prices across the country without the high cost of having to travel to different markets. On average, grain traders with cell phones had 29 percent higher profits than those without cell phones. In Niger, demand sprang up organically rather than through a specific program.</p>
<p><b>Universal education</b></p> 	<p>According to a survey of teachers in villages in four African countries, one-quarter reported that the use of mobile phones helped increase student attendance. A main factor was that teachers could contact parents to enquire about their child's whereabouts (Puri <i>et al.</i> undated). Mobile phones have also been used in Uganda to track school attendance so that school administrators can see patterns in attendance, for instance by village, by day of the week, and by season. Tracking pupils' attendance also indirectly tracks absenteeism among teachers (Twaweza 2010).</p>
<p><b>Gender equality</b></p> 	<p>A study looking at gender differences in the availability and use of mobile phones in developing countries reported that 93 percent of women who had mobile phones felt safer because of the phone, 85 percent felt more independent, and 41 percent had increased income or professional opportunities (GSM Association 2011).</p>
<p><b>Child health</b></p> 	<p>A program using text messaging to identify malnutrition among rural children in Malawi is notable for its impact on the speed and quality of data flows.<sup>28</sup> Using a system called RapidSMS, health workers in rural areas were able to transmit weight and height information in two minutes compared to two months with the previous system. The data entry error rate was significantly improved, to just 2.8 percent from 14.2 percent in the old system. The improved information flow enabled experts to analyze data more quickly and accurately, identify children at risk, and provide treatment information to health staff in the field.</p>
<p><b>Maternal health</b></p> 	<p>One of the earliest uses of mobile technology to improve maternal health took place in rural districts of Uganda in the late 1990s. Traditional birth attendants were provided with walkie-talkies, allowing them to stay in contact with health centers and obtain advice. An assessment of the program found that it led to a roughly 50 percent reduction in the maternal mortality rate (Musoke 2002).</p>

<sup>28</sup> "Malawi – Nutritional Surveillance" on the RapidSMS web site: <http://www.rapidsms.org/case-studies/malawi-nutritional-surveillance/>.

MDG	Example
<b>HIV/AIDS</b> 	<p>In Kenya, weekly text messages were sent to AIDS patients to remind them to take their antiretroviral drugs (Lester <i>et al.</i> 2010). Those who received the text messages had significantly higher rates of taking the drugs than those who did not. The study noted that SMS intervention was less expensive than in-person community adherence interventions on the basis of travel costs alone and could theoretically translate into huge health and economic benefits if scaled up.</p>
<b>Environment</b> 	<p>According to one forecast, mobile technology could lower greenhouse gas emissions 2 percent by the year 2020 (GSM Association 2009). This reduction could be met, among other ways, through widespread adoption of various mobile-enabled technologies such as smart transportation and logistics, smart grids and meters, smart buildings, and “dematerialization,” replacing the physical movement of goods and services with online transmission. Mobile phones can also be used as tools for environmental monitoring. For example, cab drivers in Accra, Ghana, were outfitted with mobile phones with GPS and a tube containing a carbon monoxide sensor to test pollution levels.<sup>29</sup></p>
<b>Partnership</b> 	<p>MDG target 8F states: “In cooperation with the private sector, make available benefits of new technologies, especially information and communications.” Mobile phone penetration in low-income economies grew from less than one per 100 people in 2000 to almost one per every three in 2010—largely as a result of private sector investment. Of some 800 telecom projects in developing countries with private sector participation between 1990 and 2009, almost three-quarters involved greenfield operations, primarily in mobile telephony.<sup>30</sup></p>

Source: World Bank 2012.

### What can governments do to foster ICT for development?

Numerous studies have found a positive relationship between ICT adoption and economic development in general. The widespread availability of ICT and mobile phone usage has created opportunities for governments to strengthen service delivery and enhance governance.

An evaluation of initial experiences suggests that the benefits accrue to those countries that put in place policies and programs that not only enable technological transformation but also support institutional reforms and process redesign through which services are delivered (World Bank 2012). Fostering an accelerated diffusion of ICT in developing countries requires undertaking country-specific analysis to take into account local conditions and translating these findings into policy actions that enable and encourage development of the demand and supply side of ICT. On the demand side, this means paying attention to affordability of mobile devices and services, while on the supply side, it requires addressing common bottlenecks such as spectrum and backbone networks..

### What can international organizations do to foster ICT for aid effectiveness?

International agencies have been increasingly interested in leveraging the rapid spread of ICT such as mobile phones to better hear the voices of beneficiaries in developing countries. By reducing barriers to accessing information, technology can facilitate transparency and contribute to accountability. ICT technology can help solicit, provide, and respond to feedback regarding projects and programs for

<sup>29</sup> [http://www.globalproblems-globalsolutions-files.org/unf\\_website/PDF/vodafone/tech\\_social\\_change/Environmental\\_Conservation\\_case3.pdf](http://www.globalproblems-globalsolutions-files.org/unf_website/PDF/vodafone/tech_social_change/Environmental_Conservation_case3.pdf).

<sup>30</sup> World Bank and PPIAF, PPI Project Database. <http://ppi.worldbank.org>. Date: 04/03/2011.

development. In addition, ICT can also help reduce the transaction costs of, for example, payments systems and improve access to finance.

Introducing new technologies to improve citizens' feedback has significantly reduced the barriers of cost, time, and space that have historically constrained direct interactions with citizens; now, it is possible to easily reach citizens to acquire their feedback (see Box 1.3). By using these ever-evolving tools, governments and international aid agencies can improve the success of feedback mechanisms to increase the effectiveness of development programs.

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### **Box 1.3: Potential Uses of Mobile Phone Surveys**

As mobile phone ownership rates have risen dramatically in Africa, there has been increased interest in using mobile telephones as a data collection platform. While face-to-face household surveys are usually expensive and time consuming, mobile phone surveys are proving to be a cost-effective, flexible, and rapid way to collect data on a wide range of topics and over time.

South Sudan and Tanzania have both piloted mobile phone surveys, with reasonable success. In South Sudan, 1,000 respondents in 10 urban areas were given cell phones in 2010, and called on a monthly basis. In Tanzania, 550 households were administered a baseline survey in 2010, and an adult respondent was selected for a weekly mobile phone survey (for 25 weeks), later administered every two weeks (for 8 weeks). Both surveys collected information on a wide variety of issues, including health, education, water, security, nutrition, travel times, prices, electricity, and governance. The surveys also asked respondents their perceptions on the most pressing problems to be addressed by the city government and their opinion about a draft constitution, and collected baseline information for large-scale programs on food fortification.

The cost per interview in each round in Tanzania was about US\$4.10-\$7.30, or about US\$0.42 per question (plus US\$50-\$150 for a baseline interview). Thus for long surveys, face-to-face interviews may be more cost-effective. However, the evidence from Tanzania and South Sudan suggests that mobile surveys can collect quality data in a timely manner that is of use to a wide range of data users. Attrition and non-response need to be dealt with at implementation, but the ability to modify surveys easily in subsequent survey rounds is a key benefit.

Lastly, the data collected in Tanzania were widely disseminated through a dedicated website, with additional attention given by a local television journalist who ensured that information was widely publicized. Accountability for public services has reportedly increased, suggesting that results need to be disseminated systematically to civil society, the media, and the government to be fully effective.

*Source: World Bank 2013.*

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# Annex 1.1: Country Classifications in World Economic Outlook, 2013

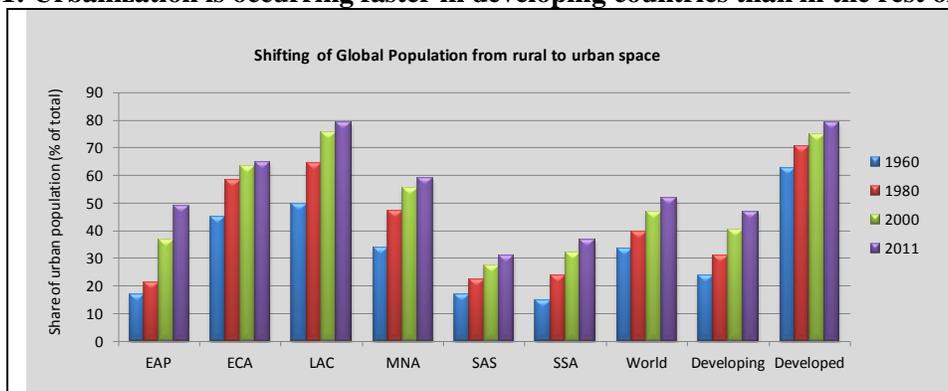
<b>Advanced Economies</b>			
Australia	France	Korea	Slovak Republic
Austria	Germany	Luxembourg	Slovenia
Belgium	Greece	Malta	Spain
Canada	Hong Kong SAR, China	Netherlands	Sweden
Cyprus	Iceland	New Zealand	Switzerland
Czech Republic	Ireland	Norway	Taiwan, China
Denmark	Israel	Portugal	United Kingdom
Estonia	Italy	San Marino	United States
Finland	Japan	Singapore	
<b>Emerging Market and Developing Countries<sup>1</sup></b>			
<b>Central and Eastern Europe</b>		<b>Sub-Sahara Africa</b>	
Albania	Lithuania	Angola*	<b>Lesotho</b>
Bosnia and Herzegovina*	FYR Macedonia	<b>Benin</b>	<b>Liberia*</b>
Bulgaria	Montenegro, Rep. of	Botswana	<b>Madagascar</b>
Croatia	Poland	<b>Burkina Faso</b>	<b>Malawi</b>
Hungary	Romania	<b>Burundi</b>	<b>Mali</b>
<b>Kosovo*</b>	Serbia	<b>Cameroon</b>	Mauritius
Latvia	Turkey	<b>Cape Verde</b>	<b>Mozambique</b>
<b>Developing Asia</b>		<b>Central African Republic*</b>	Namibia
<b>Bangladesh</b>	<b>Myanmar*</b>	<b>Chad*</b>	<b>Niger</b>
<b>Bhutan</b>	<b>Nepal*</b>	<b>Comoros*</b>	<b>Nigeria</b>
Brunei Darussalam	Palau	<b>Congo, DR*</b>	<b>Rwanda</b>
<b>Cambodia</b>	<b>Papua New Guinea</b>	<b>Congo, Republic of*</b>	<b>São Tomé and Príncipe</b>
China	Philippines	<b>Côte d'Ivoire*</b>	<b>Senegal</b>
Fiji	<b>Samoa</b>	Equatorial Guinea	Seychelles
India	<b>Solomon Islands*</b>	<b>Eritrea*</b>	<b>Sierra Leone*</b>
Indonesia	Sri Lanka	<b>Ethiopia</b>	South Africa
<b>Kiribati*</b>	Thailand	Gabon	South Sudan*
<b>Lao P.D.R.</b>	<b>Timor-Leste*</b>	<b>Gambia, The</b>	Swaziland
Malaysia	<b>Tonga</b>	<b>Ghana</b>	<b>Tanzania</b>
<b>Maldives</b>	Tuvalu*	<b>Guinea*</b>	<b>Togo*</b>
Marshall Islands*	<b>Vanuatu</b>	<b>Guinea-Bissau*</b>	<b>Uganda</b>
Micronesia*	<b>Vietnam</b>	<b>Kenya</b>	<b>Zambia</b>
<b>Mongolia</b>			Zimbabwe*
<b>Middle East and North Africa</b>		<b>Latin America and the Caribbean</b>	
<b>Afghanistan</b>	<b>Armenia</b>	Antigua and Barbuda	<b>Guyana</b>
Algeria	Azerbaijan	Argentina	<b>Haiti*</b>
Bahrain	Belarus	Bahamas, The	<b>Honduras</b>
<b>Djibouti</b>	<b>Georgia</b>	Barbados	Jamaica
Egypt	Kazakhstan	Belize	Mexico
Iran	<b>Kyrgyz Republic</b>	<b>Bolivia</b>	<b>Nicaragua</b>
Iraq*	<b>Moldova</b>	Brazil	Panama
Jordan	Russia	Chile	Paraguay
Kuwait	<b>Tajikistan</b>	Colombia	Peru
Lebanon	Turkmenistan	Costa Rica	St. Kitts and Nevis
Libya*	Ukraine	<b>Dominica</b>	<b>St. Lucia</b>
<b>Mauritania</b>	<b>Uzbekistan</b>	Dominican Republic	<b>St. Vincent &amp; the Grens.</b>
Morocco		Ecuador	Suriname
Oman		El Salvador	Trinidad and Tobago
Qatar		<b>Grenada</b>	Uruguay
Saudi Arabia		Guatemala	Venezuela
<b>Sudan*</b>			
Syria*			
Tunisia			
United Arab Emirates			
<b>Yemen*</b>			
<sup>1</sup> Countries in bold typeface are low-income developing countries eligible for financial assistance under IMF's Poverty Reduction and Growth Trust. Countries with an asterisk are included in the World Bank's list of Fragile and Conflict-Affected States.			
Source: World Economic Outlook.			

## 2. Rural-Urban Disparities

### Introduction

One of the major developments of the last three decades has been the urbanization of the developing world (Figure 2.1). In 2011, nearly 50 percent of the population in developing countries was urban compared to less than 30 percent in the 1980s. Of the global urban population of 3.6 billion, 75 percent lived in developing countries in 2011. This trend is not unique to developing countries – it also prevailed in today’s high-income countries in the 20<sup>th</sup> century. In fact, no country has graduated to a high-income status without urbanizing.

**Figure 2.1: Urbanization is occurring faster in developing countries than in the rest of the world**

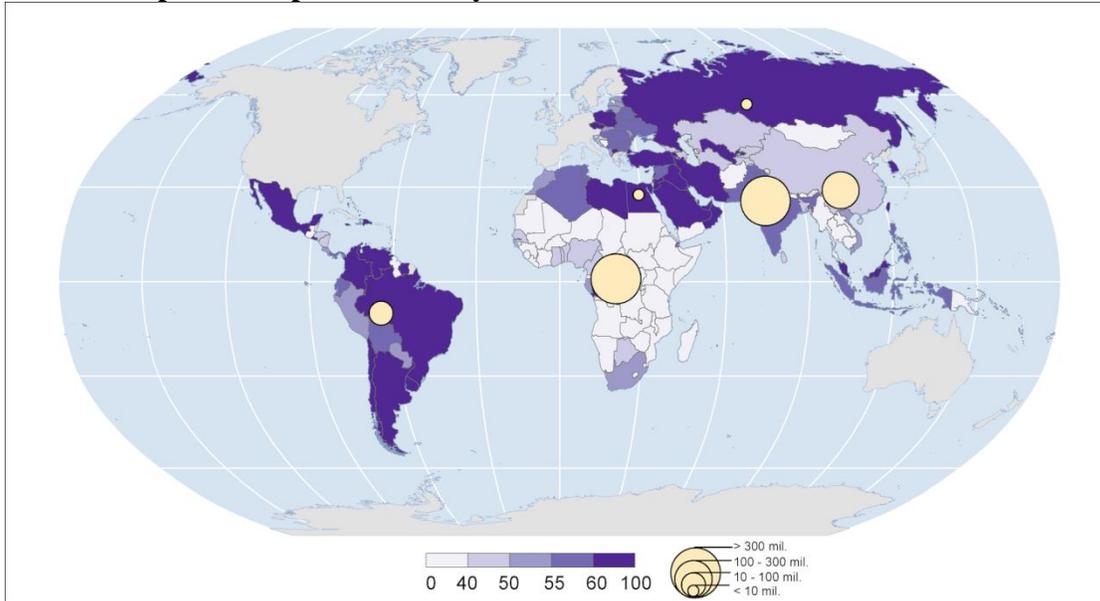


Source: World Bank 2012a.

While basically no country has reduced poverty without urbanization, it is also true that the benefits of urbanization have not ensued uniformly across countries. Close to 1 billion people live in urban slums in developing countries, including middle-income ones like Brazil and emerging ones like China and India (UN-Habitat 2010). Urban poverty also pervades smaller towns and cities. When unemployment, informality, and lack of basic services swamp the benefits offered by cities, urban poverty begins to exacerbate national poverty.

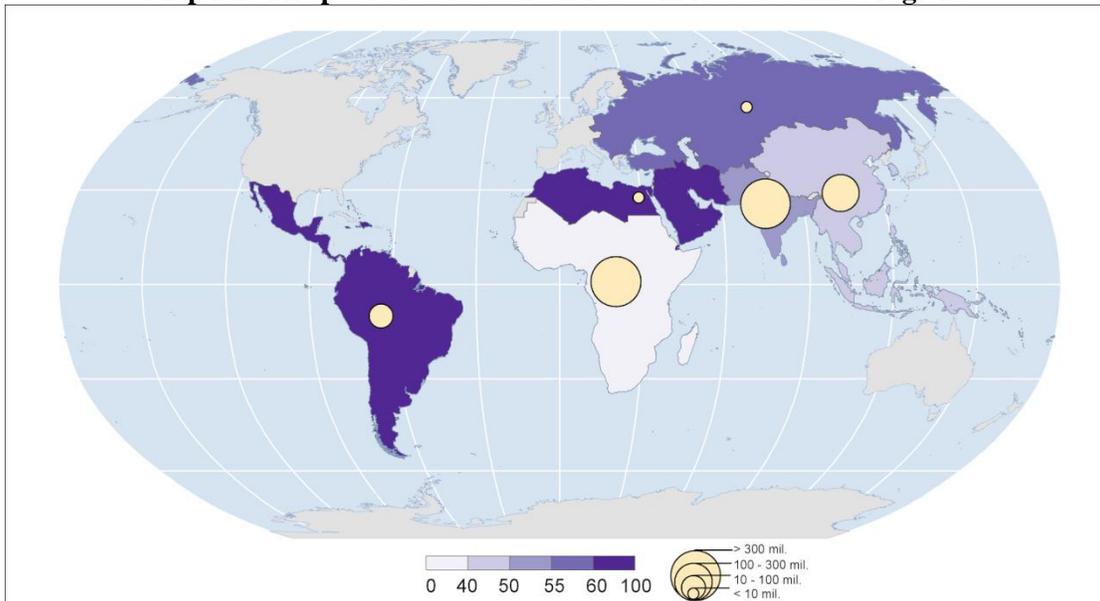
Between 1990 and 2008, overall poverty in developing countries declined (Figure 2.2). Moreover, rural and urban poverty declined in all regions but the urban population was significantly better off, especially in regions such as Latin America and the Caribbean (LAC), Middle East and Northern Africa (MNA), and Europe and Central Asia (ECA), which are highly urbanized (Table 2.1). The East Asia and Pacific (EAP) region’s success in urban and rural poverty reduction was impressive, but driven to a large extent by China’s achievement (Map 2.1). Even in the two poorest regions where the shares of the rural and urban poor in the population remained huge, the urban areas were less poor (Map 2.2).

**Map 2.1: The poor are mostly concentrated in less urbanized countries**



Source: World Bank 2013.

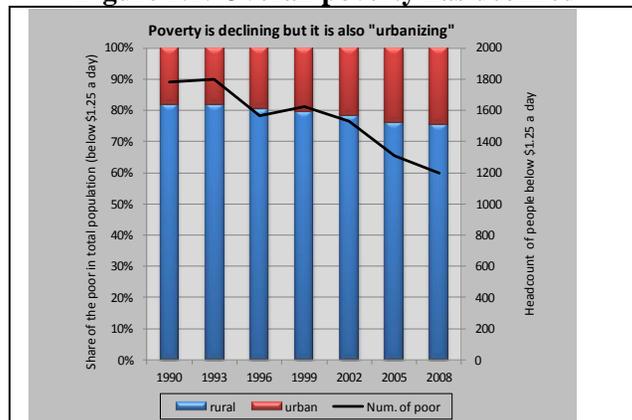
**Map 2.2: The poor are also concentrated in less urbanized regions**



Source: World Bank 2013.

In 2008, 46 percent of the rural but only 34 percent of the urban population lived on less than US\$1.25 a day in Sub-Saharan Africa (SSA). For each poor person in the urban areas of SSA, there were 2.5 as many in rural areas. In South Asia, the share of the poor in the population was 38 percent in rural areas and 30 percent in urban areas. For each poor person in an urban area, there were three poor ones in rural areas.

**Figure 2.2: Overall poverty has declined**



Source: World Bank 2013.

## Why urbanization matters for the MDGs

Urbanization matters because it can facilitate several factors that play an important role in attaining the MDG's. Urbanization can reduce poverty in two main ways: (i) through the benefits of agglomeration, cities potentially generate higher living standards for all their residents and reduce urban poverty; and (ii) through the benefits of scale economies, cities facilitate the provision of public services at a lower fixed unit cost. Cities also create revenues that governments need to foster agglomeration economies for firms and households, and finance services for rural and urban migrants. But when the positive forces driving cities are strained by excess population density, service delivery is unable to keep pace with demand and urban congestion leads to the emergence of slums. An important negative externality due to excessive urban congestion is pollution.

Agglomeration economies arise when there is a confluence of population density, which is about people, and economic density, which is about firms. The main outcome is the creation of jobs which are the center stage of poverty reduction and MDG1. According to one estimate more than 50 percent of the reduction in poverty can be attributed to an increase in labor income (World Bank 2013).

Basic MDG-related services such as infrastructure for water and sanitation, primary health care, and primary education are costly to deliver when population density is low. Higher population densities in urban areas, particularly larger cities facilitate scale economies that reduce the unit costs of service delivery and enable an expansion in coverage to serve more residents. Higher economic and population densities of urban areas are also good for governments. They generate tax revenues that are essential for financing the public goods necessary for agglomerations economies, jobs, and ultimately, poverty reduction.

Successful urbanization is reflected in dynamic cities that foster agglomeration economies. The latter thrive on large numbers of businesses and create plenty of jobs. Scale economies result when more and better jobs are created. Urbanization is inclusive and a "win-win" recipe for poverty reduction when it generates higher incomes than workers would earn elsewhere, provides access to services essential for a decent livelihood, and creates opportunities for workers to enjoy higher standards of living.

The increasing pace of urbanization in recent years has raised the hope that meeting the MDGs might become easier in developing countries. The rationale for this premise is based on the dynamics of urbanization. Barring major congestion externalities and adverse environmental effects, agglomeration economies combined with public investment in urban areas should make the goal of income poverty reduction easier in them. Even though rural areas have a larger share of the poor, the pace of rural to urban migration can lessen the pressure on rural areas. This shifts more of the weight on cities. As over half of the population in developing countries is expected to be living in cities soon (UN 2011), the onus of preserving urban prosperity and preempting uncontrolled growth in urban poverty falls squarely on cities.

## The majority of the poor remain in rural areas

The challenge of poverty reduction remains in the rural areas, and is mostly concentrated in Asia and SSA. Of the 1.2 billion poor in developing countries in 2008, 76 percent resided in rural areas. More than 420 million rural poor were in India alone, and over 210 million each in East Asia Pacific (EAP) and SSA. In other regions, where overall poverty is low, rural poverty rates exceed urban ones (Table 2.1). East Asia's success in reducing rural poverty from 67 percent in 1990 and 40 percent in 2002 to 20 percent in 2008 has been spectacular.

**Table 2.1: Rural and urban poverty is declining in developing countries**

	Share of the population below \$1.25/day											
	1990			1996			2002			2008		
	rural	urban	total	rural	urban	total	rural	urban	total	rural	urban	total
East Asia & Pacific	67.5	24.4	54.9	45.9	13.0	34.6	39.2	6.9	26.3	20.4	4.3	12.9
Europe & Central Asia	2.2	0.9	1.4	6.3	2.8	4.1	4.4	1.1	2.3	1.2	0.2	0.6
Latin America & Caribbean	21.0	7.4	11.5	20.3	6.3	10.0	20.3	8.3	11.1	13.2	3.1	5.3
Middle East & North Africa	9.1	1.9	5.3	5.6	0.9	3.1	7.5	1.2	4.0	4.1	0.8	2.2
South Asia	50.5	40.1	47.9	46.1	35.2	43.2	45.1	35.2	42.3	38.0	29.7	35.5
Sub-Saharan Africa	55.0	41.5	51.3	56.8	40.6	51.9	52.3	41.4	48.7	45.7	33.6	41.5

Source: World Bank staff estimates 2013.

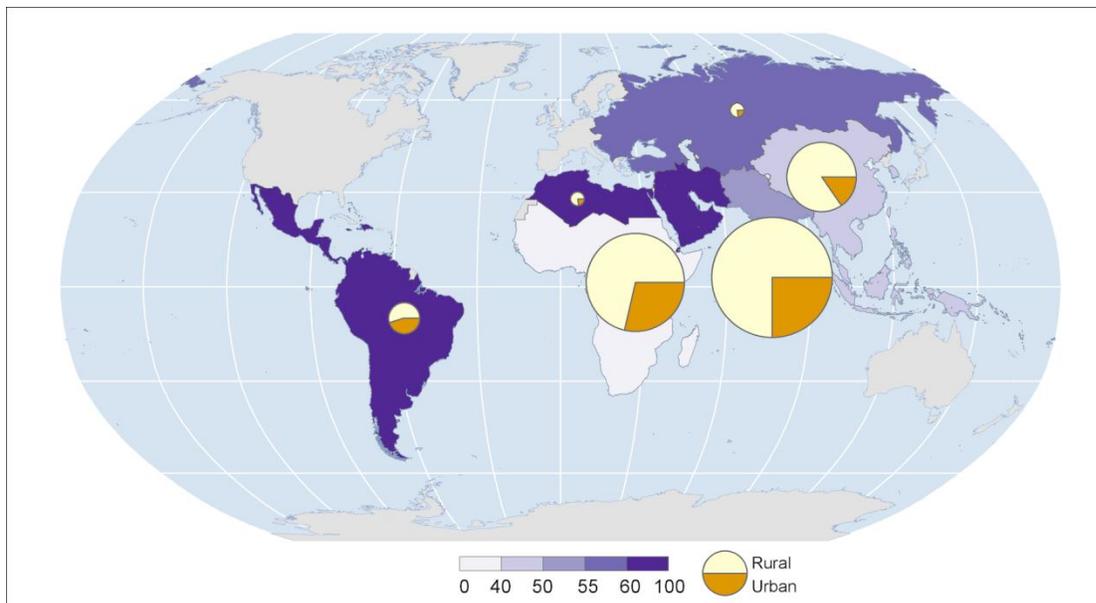
Poverty declined in rural and urban areas between 1990 and 2008. A direct though very slowly unraveling consequence of urbanization in developing countries is that poverty is urbanizing. As the share of the global population living in urban areas increases, the share of the world's poor who live in cities is also increasing. Recent World Bank (2012) and previous estimates of global urban poverty (Ravallion, Chen and Sangraula 2007) indicate that while at the beginning of the 2000s more than three-quarters of the world's poor still lived in rural areas, poverty has become more urban over time. In Latin America, this process is the most advanced: the majority of the poor in LAC now reside in urban areas (Map 2.3). In EAP, on the other hand, the process is much less advanced, with less than 10 percent of the poor living in urban areas. Urbanization of poverty in India is also underway, although it is occurring at a relatively slow rate. With its rural share of total poverty remaining at about 75 percent in 2004/05, India's situation is broadly in line with the global experience documented in Ravallion, Chen and Sangraula.

Location remains important at all stages of development, but it matters less in rich countries than in poor ones. Estimates from more than 100 Living Standard Surveys indicate that households in the most prosperous areas of developing countries such as Brazil, Bulgaria, Ghana, Indonesia, Morocco, and Sri Lanka have an average consumption almost 75 percent higher than that of similar households in the

lagging areas of these countries. In comparison, the disparity is less than 25 percent in developed countries such as Canada, Japan, and the U.S. (World Bank 2009).

According to various estimates, 60 percent of the increase in the urban population in developing countries is due to natural increase, especially in countries where fertility levels and overall population growth remain high (Chen *et al.* 1998; UN-Habitat 2008). However, in China and Indonesia, migration and reclassification of rural and urban boundaries in urban growth are estimated to account for over 70 percent of urban growth in the 1980s and about 80 percent in the 1990s.<sup>31</sup> Demographic and Health Surveys (DHS) indicate that in 26 out of the 46 countries with data available on female migrants, rural-rural migration is the most common type, and tends to be highest in Africa. Rural-rural migration is also most common among male migrants in a further seven countries, mostly located in Africa (UN-Habitat 2008). Each of these factors has vital consequences for the effect of urbanization on poverty as well as implications for policies that can make urbanization a force for poverty reduction. Another study using different methodologies finds that internal migration is significantly higher in LAC and lowest in Asia. The estimates for Africa lie somewhere in between LAC and Asia (Bell and Muhidin 2008).

**Map 2.3: Regional differences in access to sanitation are highest in the least urbanized regions (urban-rural differentials (%))**



Source: World Bank 2013.

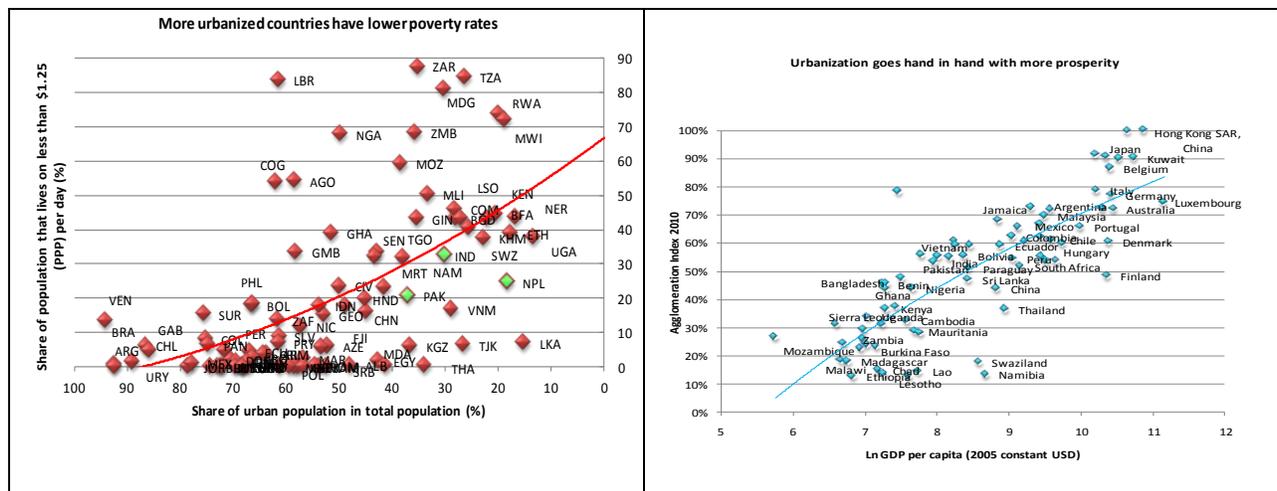
<sup>31</sup> Because the estimates are derived from census information and the definitions of urban used in the Chinese censuses have been changing, this finding should be interpreted with caution. Estimates for Indonesia indicate a steady decline in the contribution of natural increase to urban growth, from nearly 70 percent in the 1960s to 32 percent in the 1990s (United Nations 2010).

## Urbanization often fuels prosperity and dampens poverty, but not always

It is not a coincidence that the high-income countries are more urbanized: “Place is the most important correlate of a person’s welfare. ...The best predictor of income in the world today is not *what* or *whom* you know, but *where* you work” (World Bank 2009). Economic history shows that this has always been true. Before the Industrial Revolution, the world was a “rural” place, where people ploughed fields and the differences in living standards between countries were minimal. England’s Industrial Revolution unleashed a wave of industrialization that was necessarily grounded in cities or urban spaces. In fact, the changes brought about by the industrial revolution are unimaginable without cities. The mechanization of production was powered by economies of scale and a concentration of population. Rapid industrialization was accompanied by increasing urbanization and this, in turn, nurtured agglomeration economies.

Ongoing urbanization offers developing countries all of these benefits and more. Income per capita tends to rise and poverty tends to decline as the share of the urban population rises (Figure 2.3). Urbanization rates above 70 percent are typically found in high-income countries, whereas those in poorer countries, such as Ethiopia, Uganda, Laos, and Chad, are closer to 20-30 percent.

**Figure 2.3: Nexus between urbanization, poverty, and prosperity**



Source: World Bank 2012a.

The relationship between the rate of urbanization and poverty is negative (Figure 2.3). Countries with low levels of urbanization, such as those in SSA and South Asia, have significantly higher poverty rates than countries in LAC, ECA, and EAP (recall Maps 2.1 and 2.2). Rising urbanization is also positively related to increases in the proportion of GDP generated by industry and services as well as with the proportion of the labor force working in those sectors (Satterthwaite 2007). Notwithstanding the positive externalities that cities bring to economic development, urbanization is one of the important ingredients of a policy mix that fosters economic growth and prosperity. Indeed, complementary policies such as growth conducive macroeconomic policies and an investment and business-friendly climate are also necessary to be able to seize the benefits of agglomeration that cities bring.

The channels through which urbanization fosters the creation of better paying jobs are crucial to understanding why it has contributed to poverty reduction in some countries but not in others. In most

countries, structural transformation from agriculture to manufacturing and services has been in lockstep with urbanization. Invariably, industrialization is orchestrated through a light manufacturing export sector. Labor-intensive light manufacturing industries have created large numbers of better paying industrial jobs by attracting rural migrants to the urban areas (Chandra, Lin and Wang 2013). In Latin America, where the share of the urban population is over 80 percent, quantitative analysis confirms that in 10 of 18 Latin American countries, changes in labor income explain more than half the reduction in poverty, and in another five countries, more than a third (World Bank 2013).

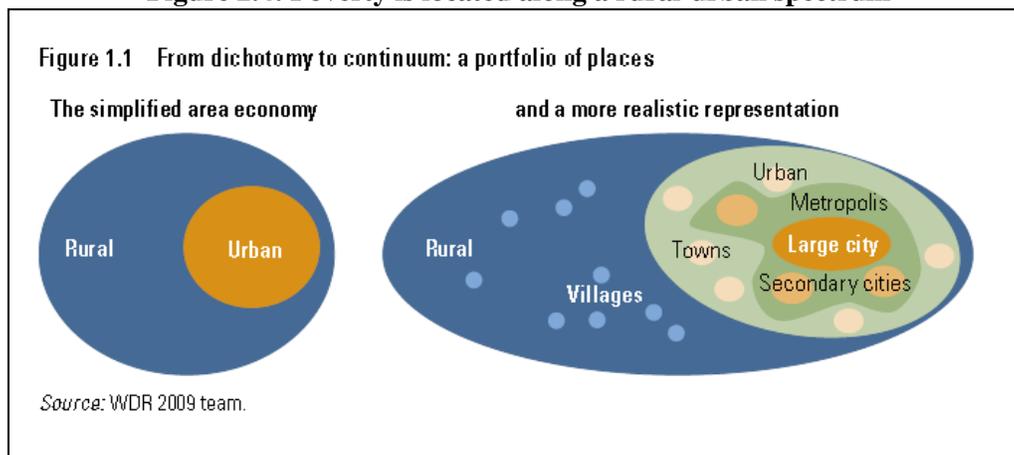
SSA’s higher poverty rates and lower income levels have created a perception that the region has urbanized without enjoying the attendant benefits of urbanization; i.e., better paying jobs, prosperity, and higher standards of living in African cities. It appears that the advantages of urbanization set in only after it has reached a critical level; countries with urbanization rates of 40 percent or less have distinctly lower income levels and higher poverty rates (Map 2.4 and Map 2.5). They also have the largest rural-urban differentials, especially in access to basic services. On average, countries with higher levels of urbanization have also made better progress in achieving more of the MDGs.

### Poverty is located along a “rural” to “urban” spectrum

Poverty is typically conceptualized as being spatially bi-polar: poor people live in either rural or urban places. In reality, poverty is located along a continuous rural-urban spectrum and the large cities where the urban population is concentrated are not necessarily places where the poor are also concentrated (Figure 2.4). As an example, while 29 percent of Brazil’s population is concentrated in the largest cities, 39 percent of the poor reside in the smallest towns.

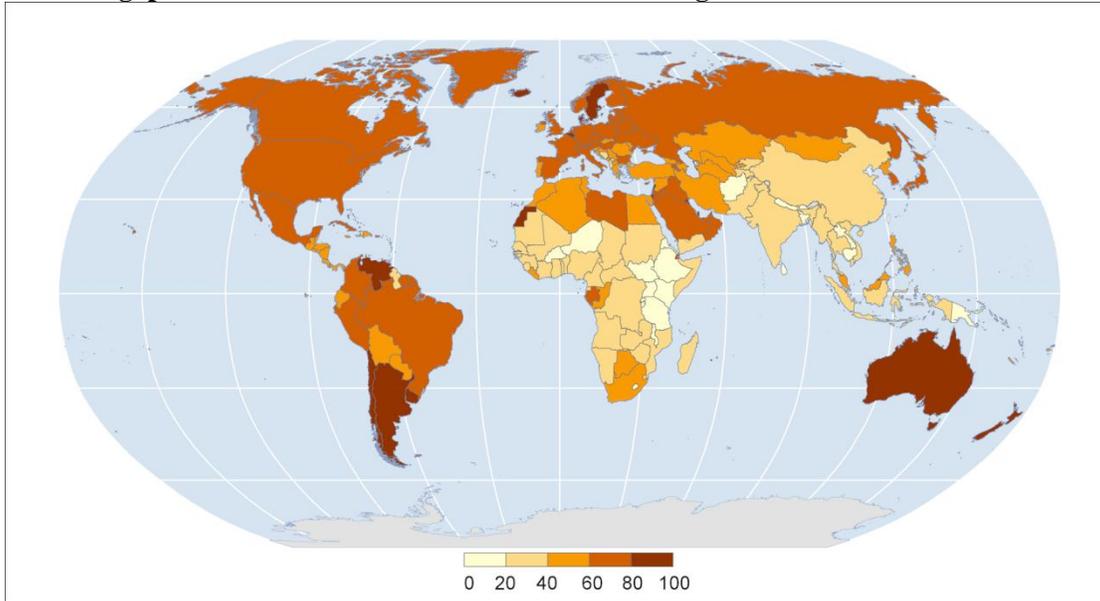
Megacities and large cities with populations of as much as 5 million or higher are the richest; smaller towns, secondary cities, and peri-urban areas are less rich; and rural areas, where a large proportion of the poor reside, are the poorest. In 2005, the share of the total world population housed in megacities and the largest cities was 17.5 percent; the share in large cities of 0.5 – 5 million was 31 percent, and the share in smaller towns with fewer than 500,000 people was 51 percent (UN 2011).

**Figure 2.4: Poverty is located along a rural-urban spectrum**



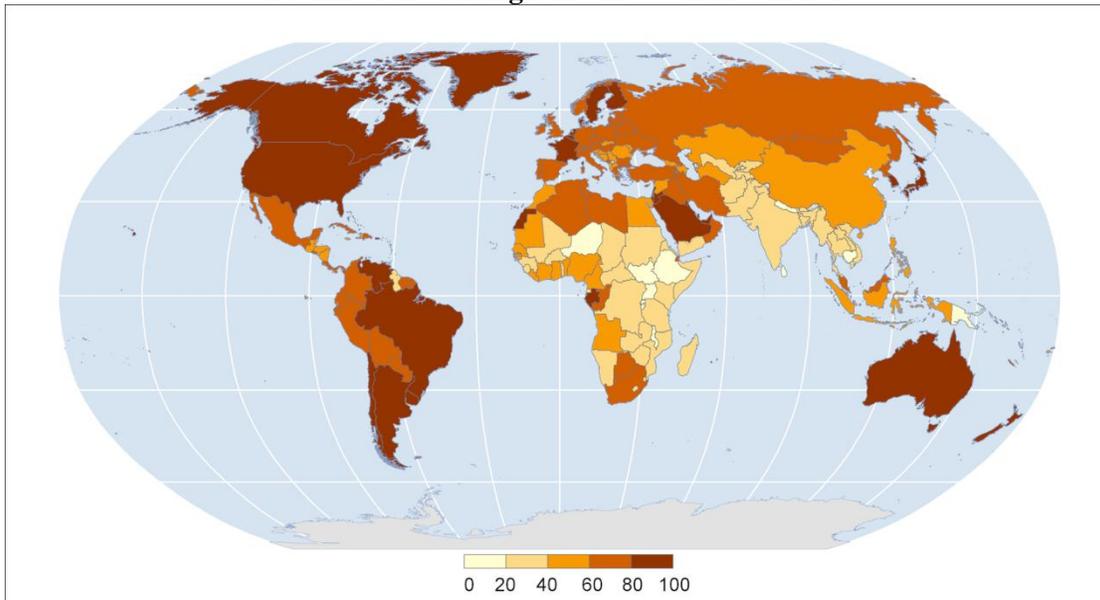
Source: World Bank 2009.

**Map 2.4: The gap between urbanization levels in low- and high-income countries in 1990 was large**



Source: World Bank 2013.

**Map 2.5: Progress in developing countries, especially East Asia, in narrowing the gap in urbanization with high-income countries in 2010**



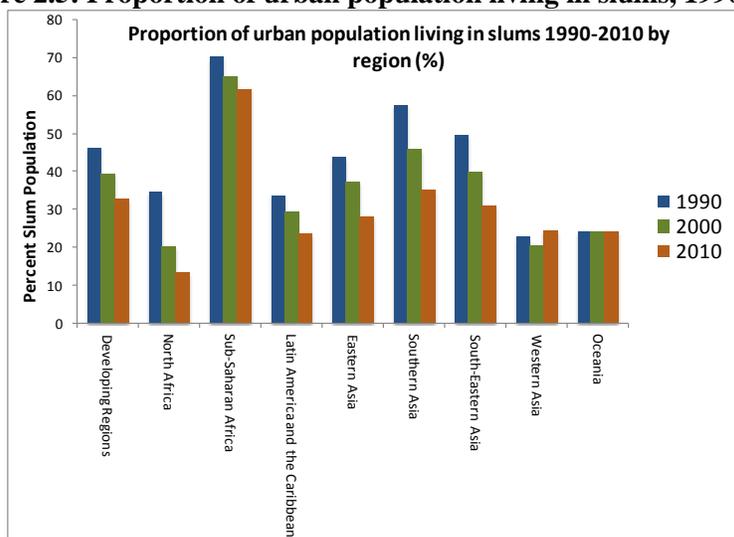
Source: World Bank 2013.

The face of urban poverty is not reflected in large or megacities alone, nor are the two equivalent. Many small countries do not have a megacity and nearly all large countries have many large cities of various sizes as well as one or several megacities. Similarly, the small towns in small countries are significantly smaller than the small towns in large countries. Smaller towns matter hugely for urban poverty reduction. In addition, while official boundaries rarely demarcate them as “slums,” the magnitude of urban cityscapes that can be considered slums is also huge. The implication of the rural-urban spectrum for the

MDGs is that all locations that house the poor or do not have access to service delivery are important and warrant attention, though their solutions for poverty reduction and service delivery may be different.

The number of slum dwellers is estimated to grow by nearly 500 million between now and 2020 (UN-Habitat 2010). The proportion of residents living in slums is already about 62 percent in Africa. Between 2000 and 2010, the increase in the absolute number of slum dwellers was driven by SSA, South-Eastern Asia, Southern Asia, and Western Asia.<sup>32</sup> While Southern Asia, South-Eastern Asia, and Eastern Asia have made impressive progress, the most significant reductions in slums have occurred in North Africa (Figure 2.5).

**Figure 2.5: Proportion of urban population living in slums, 1990-2010**



Source: UN-Habitat 2011.

In terms of sheer numbers, Asia dominates, with 61 percent of the world’s slum dwellers. Africa hosts 25.5 percent of them, and LAC is home to 13.4 percent of all slum dwellers. During 2000-2010, regional differences in the success of addressing the MDG slum target were self-evident, with some 227 million people moving out of slum conditions. However, current estimates confirm that progress in achieving the MDG target to reduce the numbers of slum dwellers has been insufficient.

If the forces of urbanization are not managed speedily and efficiently, slum growth can overwhelm city growth, exacerbate urban poverty, and derail MDG achievements. In some countries, this is already happening. The effects of urban poverty can be as dehumanizing and intense as those associated with rural poverty. Various MDG indicators showed remarkable similarities between slum and rural areas. For instance, in low-income countries such as Bangladesh, Ethiopia, Haiti, India, Nepal, and Niger – countries where poverty is seen as primarily a rural phenomenon – four out of every 10 slum children are malnourished, a rate comparable to that found in the rural areas of these countries. Likewise, in cities such as Khartoum and Nairobi, the prevalence of diarrhea is much higher among slum children than among

<sup>32</sup> It should be noted that estimation of a complex concept such as “slum” will always be somewhat arbitrary and definition driven. By using a consistent definition in the same places at different points in time, genuine changes may be observed – particularly when broad averages are “drilled down” to examine the underlying changes in real conditions in individual cities.

rural children. In slums, child deaths are attributed not so much to lack of immunization against measles, but to inadequate living conditions, such as indoor air pollution or lack of access to safe water and sanitation, which lead to water-borne and respiratory illnesses among children (UN-Habitat 2008).

## Unveiling the face of urban poverty – cities and small towns

Urban poverty is not homogeneously distributed across a country's cities and towns (Table 2.2). With the aid of new analytical techniques that combine census and household survey data, researchers have constructed "poverty-city size gradients" that shed interesting insights on the relationship between poverty and city size (Elbers, Lanjouw and Lanjouw 2002 and 2003). Recent research for a large number of countries shows that urban poverty is clearly lowest in the largest cities (Ferré, Ferreira and Lanjouw 2012). In the 1970s and 1980s, better provision of services in urban areas of developing countries led to the view that governments had an "urban bias" (Lipton 1977). In recent years, studies that have analyzed the poverty-city size gradient have raised similar questions: is there a "metropolitan bias" in the allocation of resources to larger cities at the expense of smaller towns (Table 2.3)?<sup>33</sup>

In a fairly large number of countries in Asia, Latin America, Africa, the Middle East, and Europe and Central Asia, not only is the incidence of poverty higher in small cities and towns, but these urban centers also account for the largest share of the urban poor. In principle, if large metropolitan cities account for a sufficiently large share of the urban population, then even if the incidence of poverty in such centers is lower than in smaller towns, they could account for the bulk of the urban poor. However, even in such countries as Brazil and Thailand, with well-known megacities such as Sao Paulo, Rio de Janeiro, and Bangkok, the share of the urban poor residing in small- and medium-sized towns exceeds that in the largest cities. In Brazil, 79 percent of the urban poor reside in small- and medium-sized towns, while in Thailand the fraction is 88 percent. Lower rates of poverty in large cities are consistent with stories of urban growth being driven by agglomeration externalities.

Poverty is worse in smaller towns. Whether urban residents are concentrated in the largest cities or more spread across various city sizes, poverty rates are clearly lower in the largest cities. Findings from a study of eight developing countries (Albania, Brazil, Kazakhstan, Kenya, Mexico, Morocco, Sri Lanka, and Thailand) show that with the exception of Mexico, the urban population was concentrated in the largest cities but the urban poor were dispersed along a continuum of medium, smaller, and extra small towns (Table 2.3). In Brazil, one of the most urbanized developing countries, 83 percent of the population is settled relatively evenly along the urban spatial spectrum – 22 percent in megacities, 24 percent in medium-sized cities, and 28 percent in the smallest towns. Brazilian poverty has a predominantly urban face, though not in its megacities – 72 percent of the poor live in urban areas, but surprisingly, only 9 percent reside in the megacities of Rio de Janeiro and Sao Paulo. The rest of the poor are concentrated in medium (17 percent) and extra small towns (39 percent).

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<sup>33</sup> Ferré *et al.* (2009) suggest that while "urban bias" was a much discussed concern during the 1970s and 1980s, following Lipton (1977), the idea of a "metropolitan bias" has not been widely emphasized in the poverty measurement literature. This is likely due, at least in part, to scant availability of data on living standards across finely defined city-size categories.

**Table 2.2: The primacy of smaller towns matters for urban poverty**

City Size Class	Number of agglomerations			Population in urban areas			Percentage of urban population		
	1975	2005	2010	1975	2005	2010	1975	2005	2010
10 Million or More	3	19	23	53185	284943	352465	3.5	8.9	9.9
5 to 10 million	14	33	38	109426	229718	266078	7.1	7.2	7.5
1 to 5 million	144	340	388	291663	667652	759919	19	20.9	21.4
500,000 to 1 million	224	463	513	155770	317166	353802	10.1	9.9	9.9
Fewer than 500,000	NA	NA	NA	927625	1698055	1826313	60.3	53.1	51.3

Source: UN 2011.

**Table 2.3: The poor are disproportionately concentrated in smaller cities and towns**

	Urban	XL	L	M	S	XS
<b>Albania</b>						
Population share	0.42			0.15	0.13	0.14
Share of the Poor	0.31			0.11	0.09	0.11
<b>Brazil</b>						
Population share	0.83	0.22	0.07	0.24	0.01	0.28
Share of the Poor	0.72	0.09	0.06	0.17	0.01	0.39
<b>Kazakhstan</b>						
Population share	0.57	0.08		0.29	0.05	0.15
Share of the Poor	0.43	0.01		0.21	0.05	0.15
<b>Kenya</b>						
Population share	0.19	0.07	0.02	0.03	0.02	0.04
Share of the Poor	0.16	0.06	0.02	0.03	0.02	0.04
<b>Mexico</b>						
Population share	0.6	0.27	0.13	0.11	0.04	0.06
Share of the Poor	0.39	0.16	0.06	0.07	0.03	0.07
<b>Morocco</b>						
Population share	0.51	0.12	0.09	0.27	0.03	0.01
Share of the Poor	0.34	0.03	0.07	0.2	0.03	0.01
<b>Sri Lanka</b>						
Population share	0.12		0.03	0.03	0.02	0.04
Share of the Poor	0.05		0.01	0.01	0.01	0.02
<b>Thailand</b>						
Population share	0.31	0.12		0.03	0.02	0.14
Share of the Poor	0.17	0.01		0.01	0.01	0.13
<b>Notes:</b>						
Population share: Proportion of the population living in each category: urban, XL,L,M,S,XS.						
Share of the Poor: Proportion of the country's poor living in each category: urban, XL,L,M,S,XS.						
XL: >1,000, L: 500-1,000, M: 100-500, S: 50-100, XS: <50 ('000 inhabitants).						
Source: Ferre, Ferreira and Lanjouw (2012)						

Source: Ferre, Ferreira and Lanjouw 2012.

### Sub-Saharan Africa: urban poverty is low and concentrated in the largest cities

An ongoing study of 12 SSA countries shows that although the poverty-city size gradient observed in African countries is similar to that seen in developing countries elsewhere, the African experience is different (Lanjouw forthcoming). Unsurprisingly, poverty is a rural phenomenon in SSA. The share of the poor in rural areas ranges from 68 percent in CAR to 90 percent in Mali and Swaziland to 95 percent in Malawi. The face of urban poverty in SSA is distinct because it reflects a “largest city” model; i.e., the

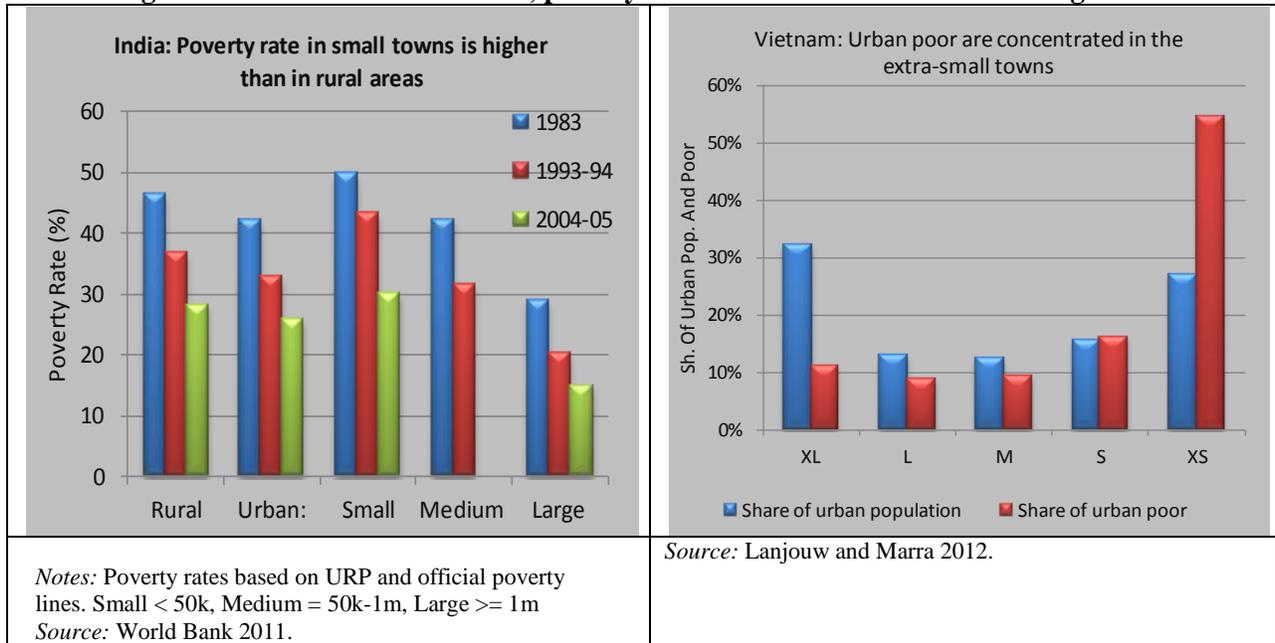
largest city accounts for a disproportionately large share of the total urban population, and hence also for the bulk of the urban poor. For example, in Malawi, Gabon, and CAR, the largest city size category accounts for more than half of each country's urban poor. The corresponding share is 40 percent in Swaziland, Senegal, Niger, Guinea, and Sierra Leone. In most African countries, "urban" thus implies similarity to the "largest city," usually the capital. In Mali, Malawi, Niger, and Togo, towns with between 5,000-100,000 inhabitants have a population share between 2-6 percent. This pattern is different from other predominantly "rural" developing countries such as India and Vietnam. The primary reason for urban poverty's relative concentration in the capital is the paucity of better paying non-farm jobs in smaller towns. Spatial transformation of the population from rural to urban in Africa has stalled in large part because the structural transformation from agriculture to industry (manufacturing and services) has been slow to emerge. Manufacturing, especially agro-industry, and related service sectors have an average share of only 10 percent of the economy in SSA and industries related to them generally locate in the largest city providing access to services.

### **South and East Asia: urban poverty is huge and largely in small towns**

In both South and East Asia, despite their megacities and sprawling slums, urban poverty is firmly located in smaller towns, not in big cities. Unfortunately, due to data limitations, reliable estimates of the share of poverty in slums are not available. South Asia's poverty challenge has two dimensions: (i) the majority of the poor reside in rural areas where poverty is severe regardless of the metric used to measure it; in 2008, over 420 million poor resided in rural areas compared to 141 million in urban areas; and (ii) poverty rates in smaller towns are significantly higher than in megacities. Various factors explain why this is so.

Recent research in India, for example, indicates that while poverty is primarily a rural phenomenon at the aggregate level, urban poverty is becoming a larger problem, and within urban areas, poverty is concentrated in smaller towns. The poverty-city size gradient is steep in India. It bears noting, though, that in India, even a "medium" size city has a population of close to 1 million, while in Vietnam, the population of an average small town is about 85,000. The poverty rate for rural areas in India was 28 percent in 2004-05, compared to 26 percent in urban areas. Among urban areas, at 30 percent, poverty rates were highest in small towns (population less than 50,000) compared to 15 percent in large cities with a population of 1 million or more. (Figure 2.6) (World Bank 2011; Lanjouw and Marra 2012).

**Figure 2.6: In India and Vietnam, poverty in small towns is worse than in large cities**



More than 200 cities and towns dot Bangladesh and Pakistan, yet urbanization in both of these countries is dominated by a few large metropolitan cities with a population of more than 1 million. For example, Dhaka and Chittagong account for 43 percent of Bangladesh’s urban population; in Pakistan, eight cities with a population of more than 1 million account for 58 percent of the urban population. Another 24 percent of the urban population in Pakistan resides in 48 cities with populations of 100,000 to 1 million.

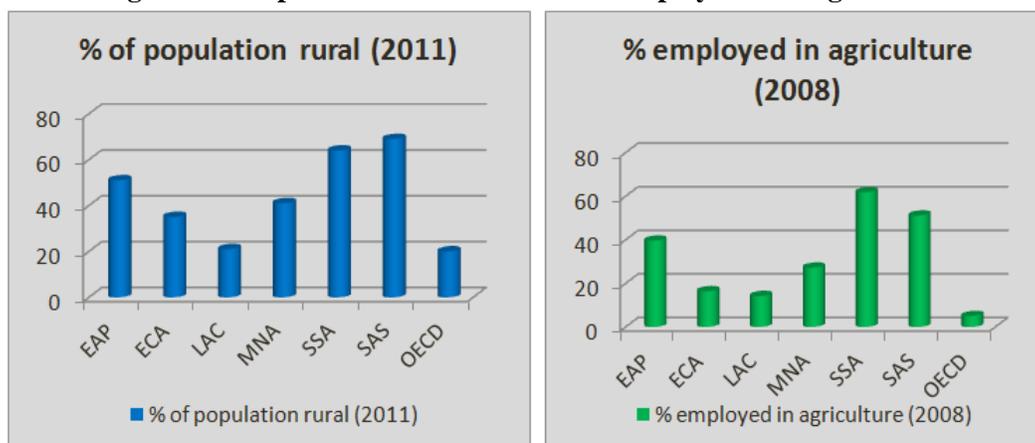
Evidence from these countries reveals that the incidence of poverty is highest in rural areas, followed by smaller towns and cities, and is lowest in metropolitan areas. The poverty incidence in Bangladesh is about 26 percent in metropolitan areas, about 38 percent in peri-urban areas and smaller cities, and 43 percent in rural areas. A similar pattern is observed in Pakistan (Deichman, Shilpi and Vakis 2009). In Vietnam, the nexus between urban population and urban poverty is mirrored in a remarkable U-shape (right panel of Figure 2.6). Two megacities, Hanoi and Ho Chi Minh, with a population of over 4 million each, are home to about 30 percent of urban residents but only about 10 percent of the poor. In comparison, the 634 smallest Vietnamese towns, with an average population of about 10,000, host more than 55 percent of the urban poor (World Bank 2011; Lanjouw and Marra 2012).

Small towns can play an important role in arresting the “urbanization” of poverty if policies that improve residents’ access to basic services and nurture economic activity are implemented. The reality of the poverty-city size gradient shows that policies that improve service delivery and foster nonfarm job creation in small towns and peri-urban areas, can offer rural migrants better livelihoods. In countries where population density is high in smaller towns, it is possible that the scale economies are sufficiently large to make service delivery cost-effective. Smaller towns can also serve as a catchment area for the rural poor when they want to migrate in search of better jobs and services but don’t want to go as far as large cities. In small towns located in the vicinity of rural areas, policies that promote non-farm jobs can be instrumental in reducing rural poverty.

## Linkages between urbanization and rural poverty

There are multiple linkages between urbanization and poverty reduction. Rural-urban migration and non-farm economic activity are two of them. Intricate linkages between rural and urban sources of growth generate additional potential for poverty reduction.

**Figure 2.7: Population in rural areas and employment in agriculture**



Source: World Bank 2012.

A concentration of a large share of the rural population in agriculture has gone hand in hand with poverty in most developing countries. In developed countries, about 20 percent of the population lives in rural areas and 5 percent is dependent on agriculture for employment. In South Asia and SSA, more than half of the labor force is employed in agriculture mostly as unpaid family workers (Figure 2.7). Indeed, in the absence of adequate safety nets, agriculture is an important fallback option for family members who lose their job due to economic shocks or other crises. A consequence of limited job opportunities outside agriculture in the poorer developing countries is that agriculture is forced to absorb extra labor, which leads to underemployment, low labor productivity, and thus low farm incomes.

There are intricate linkages between rural and urban areas, and what happens in one area affects the other. Rural growth contributes to urban growth and vice versa, but rural growth cannot occur without good access to (urban) markets and vibrant farm and nonfarm activities. East Asia's rapid population and economic growth in urban areas was preceded by successful land reforms and green revolution in agriculture though there were exceptions to this pattern as well (e.g., Korea) (Gollin 2009; Mellor 1996). Rural growth helped to lower food prices and real wages for urban areas, and created demand for urban goods. Rising income in rural areas allows rural households to invest in their own businesses and also their children's health and education, preparing them better for urban jobs. This is not happening as fast in SSA and South Asia where rural poverty is most pervasive.

There is a large literature documenting how agricultural productivity as well as commercialization and specialization are adversely affected by lack of market access. da Mata *et al.* (2007) examined the growth of cities in Brazil, a highly urbanized developing country. They found that city growth has been positively associated with market potential in surrounding rural areas (measured by rural per capita income weighted by distance). Using household data from Nepal, Emran and Shilpi (2012) analyzed the relationship

between market size defined as the size of the population in a certain area and the distance of that area to the closest market. They found that the crop portfolio of a village becomes more diversified with a decrease in the extent of the market up to a threshold, after which it becomes specialized. They also found that agricultural commercialization declined with a decline in the extent of the market.

## **Urban growth can reduce rural poverty through rural–urban migration**

In most developing countries, especially low-income ones, urban areas symbolize many good things. They offer better jobs, sufficient food for children, a respite from toiling on a farm without a decent income, safe drinking water, and shorter distances to doctors and other health care facilities. These attributes explain why people from rural areas are “pulled” to cities from rural villages. The “pull” effects of urbanization are an important source of rural poverty reduction and work through the dynamics of rural-urban migration. Through the natural movement of people, especially the poor, migration has the potential to move large numbers of poor people to urban areas where they have better economic opportunities and access to basic services which are most cost-effectively delivered in places where population density is high and scale economies exist. Migration is especially useful in rural areas where the sources of farm and non-farm incomes are often limited. In countries where urban areas have benefited from structural transformation, rural-urban migration has been instrumental in moving large numbers of the rural poor to the cities. The extent to which migration alleviates rural poverty depends upon a variety of factors.

In SSA, poverty remains for now a predominantly rural phenomenon. As the region is largely land-abundant and sparsely populated, delivery of public services to a large number of the rural poor is costly. A relatively small proportion of the population resides in urban areas and is concentrated in the largest cities. However, rural to urban migration is playing a prominent role in reducing rural poverty. In Tanzania, between 1991-94 and 2010, more than 50 percent of the rural population migrated to urban areas. For over 45 percent of male but only 15 percent of female migrants, the main motivation for migration was to look for better paying work in urban areas (Weerdt 2012). Located near Lake Victoria in the Kagera region in Northwestern Tanzania, bordering Burundi, Rwanda, and Uganda, the mainstay of more than 80 percent of rural residents is agricultural production of food and a few cash crops. On average, consumption levels almost doubled over 19 years. For non-migrants, consumption increased by more than 40 percent, but for migrants who left Kagera, consumption tripled. Nearly all migrants escaped poverty while for those who remained in rural areas, poverty declined only modestly (Weerdt and Dercon 2011). Were SSA to urbanize rapidly, rural-urban migration could play a similarly useful role in enabling the rural poor to escape poverty.

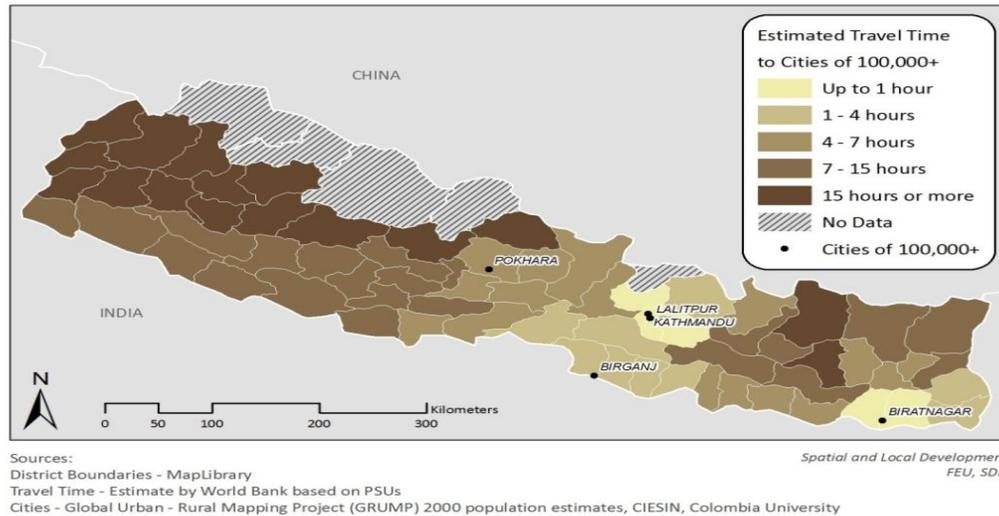
Given extreme and pervasive rural poverty, why do large cities not attract the rural poor in large numbers? Although there is migration from rural to urban areas in South Asia, its magnitude is limited. The rural poor prefer to migrate to smaller towns in their vicinity where poverty is higher than in large cities. Migration to poor smaller towns curbs the potential of urbanization as a pathway out of poverty for the rural poor. Unraveling the causes that dampen the incentives for migration is necessary for designing policies that can spur the process and to help close the gap in poverty between rural and urban areas. Otherwise, inertia in large-scale rural and urban poverty will persist.

Rural-urban migration is limited when land markets are distorted. Farmers in countries as diverse as Sri Lanka and Ethiopia can lose their land if they are not cultivating it, while also being prohibited from selling their land. The threat of losing user rights to land is also embedded in the communal property rights systems found in most African countries. The inalienability of land rights under the household responsibility system in China increased migration costs, slowing its sectoral transformation (Yang 2011). Removal of the control in 1988 was followed by a surge in migration, although most rural-to-urban migrants were “floating populations” whose families remained in rural areas to retain the households’ land earnings. Emran and Shilpi (2011) found that land sales restrictions in Sri Lanka reduced migration out of rural areas, keeping wages low and hence poverty high in rural areas. About 10 percent of all cultivated land is subject to sales restriction, as embedded in Sri Lanka’s Land Development Ordinance. A 1 percentage point increase in land under restriction leads to a 3.7 percent decrease in female wage and a 1.7 percent decrease in male wage. Such restrictions deter migration to cities where the poor can enjoy better livelihoods.

In South Asia in particular, the rural poor choose to migrate to small towns so that they can stay closer to home to mitigate the potential loss of agricultural income from migrants’ farms. The prospect of losing ownership of land due to distorted land markets stalls migration. Often migrants leave their land to be farmed by their relatives when they leave for the city and lose ownership if they have gone too far for long periods. Other reasons are wanting to stay close to family in the village. Informal barriers such as language, ethnicity, and religious differences also impede migration. For example, Munshi and Rosenzweig (2009) found that strong mutual assistance networks among sub-caste groups in the place of origin strongly discourage migration in India. Much of the migration in India is from rural to rural areas because more than half of the migrants are women who move primarily because of family reasons (marriage). Work migration is more prevalent among men. In some countries, higher costs of living in the larger cities are a deterrent.

Factors that can facilitate migration include investment in education and health to enable migrants to contribute to urbanization and reduce rural poverty. Migration is not happening fast enough to reduce the pressure of labor force absorption in agriculture in the short to medium term (Shilpi 2013). The removal of official direct and indirect restrictions on labor mobility will help to reduce poverty and improve access to basic services emphasized in the MDGs. Even in countries with no direct or indirect barriers to migration, investment in education – an important MDG – is needed to improve labor mobility.

**Figure 2.8: Travel time to cities in Nepal**  
**Travel Time to Cities of 100,000+ Population**



Source: Dudwick *et al.* 2011.

Other factors that can facilitate migration include proximity to paved roads and areas with higher housing premiums because they provide better access to services. When migrants move to cities for primarily better access to services (“push effects”), congestion in cities can worsen and exacerbate urban poverty, as is evident from the presence of slums. When migrants move in the hope of finding better jobs (“pull factors”), migrants can contribute to urbanization if they have the human capital necessary to find a better job. In this context, if people are migrating from villages to gain access to services (e.g., electricity or sanitation), policy makers can prioritize provision of these services in areas where it is less costly to provide them. In Nepal, where limited agricultural potential in the hills and mountains makes migration an important livelihood strategy, migrants value proximity to paved roads and areas with higher housing premiums (Figure 2.8). Paved roads reduces the time and costs of accessing schools, health facilities, and markets. Reflecting that, housing premia are higher in areas with better access to services and amenities. It has been found that poor migrants are willing to accept lower wages to get access to better services (Fafchamps and Shilpi (forthcoming); Lall, Timmins and Yu 2009).

Free mobility of labor eliminated welfare differences for unskilled and poorer workers/households. This is supported by evidence from Mozambique and Uganda (Dudwick *et al.* 2011). Many developing countries institute land market policies in rural areas to discourage migration to urban areas but these worsen poverty. Migration is officially restricted in a large number of developing countries, the most notable examples being China (Au and Henderson 2006), Vietnam, and Ethiopia. To discourage migration from rural areas, many countries simply resort to not providing basic water and sanitation services to poorer urban areas, often the first destination of rural migrants. For example, governments in the richer and larger localities in an urban area in Brazil reduce provision of water and sewerage connections to the smaller houses in which poorer migrants would live to discourage in-migration and deflect migrants to other localities (Feler and Henderson 2011).

Migration can be a force to reduce rural poverty and promote access to basic services but the magnitude of migration differs between countries. Policies to foster migration are important to enable the poor to

migrate from poor to rich areas, and governments can help reduce rural poverty by making migration more efficient. Equipping a citizen with human capital assets while she is still in a rural area will increase the chance that her job search in the city is successful. Similarly, connecting isolated rural areas with urban markets through better roads can increase the rural poor's ability to migrate to smaller towns where there are non-farm opportunities. Many developing countries have instituted land market policies in rural areas to discourage migration to urban areas. Restrictions in the land market are detrimental not only to agricultural productivity growth but also hinder diversification into non-farm activities that have higher returns.

Many governments have placed restrictions on rural-urban migration to pre-empt overcrowding in cities. These restrictions prevent the rural poor from benefiting from the advantages of urbanization. However, migration cannot be leveraged uniformly by policy makers to equalize the benefits of urbanization between rural and urban areas in every country. In countries in LAC where its magnitude is relatively high, and population density is high in larger cities, migration can indeed enable the rural poor to benefit from moving to large cities. Higher population density in cities can accelerate scale economies that make the extension of basic network services (piped water, sewers) more affordable for resource-constrained governments. However, in countries in South Asia, where rural-urban migration is low, its equalizing potential will be limited. Economic growth is often concentrated geographically and described as being located in a leading region complemented with a lagging region where growth is stagnant. MDGs' related issues in leading and lagging regions are quite similar to those for rural and urban areas. In Uganda, where the leading lagging region issue surfaces in policy discussions, the test the government faces is to allow, if not encourage, the concentration of economic activity while achieving a convergence of living standards and delivery of basic services like the MDGs across space (Box 2.1).

### **Box 2.1: Is the Policy Agenda Different for Leading-Lagging Regions? The Case of Uganda**

The challenge of economic and social development is that economic growth is often concentrated geographically, will lead to specialization, and induces migration. Hence, certain regions lead economically, while other regions lag. Governments face a test to allow, if not encourage, the concentration of economic activity while achieving a convergence of living standards and delivery of basic services like the MDGs across space.

Uganda realized that its current and future development path is dominated by these types of challenges. Uganda has made commendable progress in raising income welfare at the national level, but there are gaps with some geographical pockets (lagging regions) not improving as much as others (leading regions). The Midnorth, Northeast, and West Nile are lagging behind in terms of incidence of poverty, even as poverty was declining at a faster rate than the national average in the latter part of the 2000s. Kampala is well ahead of other regions, with the poverty head count declining from 14.0 percent to 4.0 percent between 1992 and 2010. Similar differentials are observed with respect to other measures of welfare. Consequently, in collaboration with the World Bank,<sup>34</sup> the Government of Uganda is trying to prioritize policies that generate the highest payoff for economic efficiency and provide geographic equity at the same time.

The Uganda Promoting Inclusive Growth country report identifies various policy areas that can make possible the integration of lagging and leading regions. The first policy area is one that facilitates integration through *better labor mobility*, which calls for emphasis on equipping people with a minimum level of education and skills such that people are able to take on the more demanding jobs in the leading regions. The second one is *making land, a physically immobile asset, more fluid* and its tenure more secure, allowing farmers to raise productivity within agriculture and to facilitate labor movement from agriculture to non-agricultural activities, as leasing and renting of land becomes feasible. One important policy action identified in Uganda is the development of a well-functioning system of conflict and dispute resolution through a clear legal and institutional framework to promote security and encourage development of the rental market. The third policy area is to support integration through *improved connectivity*, which allows for improved mobility of people, products, and technology. Isolation can confine producers to small markets and restrict them to inputs available in their geographic location. By enhancing connectivity, producers and firms can increase market size, and consequently their ability to exploit economies of scale, draw from a larger pool of workers, and have greater access to raw materials and equipment. Finally, underpinning effectiveness of all the above areas of focus is *broadening coverage, quality, and accessibility of MDG-related social services across leading and lagging regions*. This will empower people seeking economic opportunity, and reduce congestion costs caused by migration due to lack of access to social services in lagging areas.

Not surprisingly, the expected impact of public expenditure on development needs to guide Uganda's policy makers in their decision to prioritize and sequence the various policies competing for the limited resources available. For instance, geographical prioritization of investments in (social and/or physical) infrastructure is complicated if the trade-offs between economic efficiency and welfare gains are taken into account. On one hand, economic returns suggest that investing in physical-or place-specific economic infrastructure should be prioritized in leading areas to exploit economies of scale and agglomeration, build density, and accelerate growth. As for many other countries, Uganda firms locate where they can benefit from agglomeration economies, suggesting prioritization of investments in infrastructure where these clusters are already forming in the Southern-Eastern corridor of Uganda. On the other hand, investments in social infrastructure yield positive returns across all regions, emphasizing the need for equitable provisions of social services across geographical space.

This policy focus is not much different from the policy agenda advocated in the GMR, which can facilitate progress towards the MDGs through better use of policies that assist the urbanization process given the advantages that urban areas have regarding income and thus poverty and MDG-related outcomes that are linked to better service delivery in urban areas.

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<sup>34</sup> Uganda Promoting Inclusive Growth: Transforming Farms, Human Capital and Economic Geography, 2012.

## Non-farm employment and rural poverty

Rural areas also undergo profound transformation as workers move out of agriculture to non-farm activities. Indeed, throughout developing world, non-farm sectors have been becoming increasingly important source of employment and income in rural areas (Lanjouw and Lanjouw 2001; Reardon, Haggblade, Hazell and Reardon 2006). The non-farm sector accounts for 25–50 percent of rural employment in South Asian countries. For SSA, Fox and Sohnesen (2012) estimate this share for Burkina Faso, Cameroon, Republic of the Congo, Ghana, Mozambique, Rwanda, Tanzania, and Uganda and find that it varies from 20–33 percent of total employment.

On average, returns to labor are higher from non-farm activities compared with farming, and the incidence of poverty is lower among households with access to non-farm employment than among households dependent purely on agriculture. Foster and Rosenzweig (2004) found that growth in non-farm activities – primarily manufacturing -- in rural areas in India and the impacts of non-farm employment growth on poverty reduction were much larger than those of agricultural productivity growth.

The agglomeration economies associated with urbanization strongly affect the location of non-farm activities. Manufacturing and salaried non-farm jobs in developing countries usually follow specialization patterns (von Thunen). Salaried and wage work, including hierarchical work (e.g., clerks, managers, etc.), are concentrated within and around large cities, and decline precipitously within 3-4 hours of travel time from the city (Fafchamps and Shilpi 2003 and 2005). The concentration of better paid non-farm activities near larger cities is confirmed for Bangladesh (Deichmann, Shilpi and Vakis 2009) and Indonesia (Yamauchi *et al.* 2011).

Growth of non-farm activities is often driven by growth in agricultural productivity in the initial stage because of production, consumption, and labor market linkages between the farm and non-farm sectors (Haggblade, Hazell and Dorosh 2006). Smaller towns in the vicinity of rural areas are usually the most popular locations for non-farm activities. However, non-farm economic opportunities that can alleviate rural and small town poverty fail to emerge if access to markets in large urban centers do not exist. Deichmann *et al.* (2009) found that lack of connectivity is doubly damaging for areas with higher agricultural potentials in Bangladesh. It not only depresses growth in agricultural productivity but also discourages growth of better paying non-farm activities directly and indirectly (due to agricultural linkages). Other factors that foster non-farm activity include education (Lanjouw and Lanjouw 2001; World Bank 2008; Reardon, Haggblade, Hazell and Reardon 2006; Fox and Sohnesen 2012) and access and reliability of electricity. The latter two are found to be among the topmost constraints to non-farm activity in rural areas and small towns in Sri Lanka, Tanzania, Bangladesh, Indonesia, and many more countries (World Bank/IFC, Investment Climate Surveys).

Restrictions in the land market are detrimental for diversification into non-farm activities. Do and Iyer (2008) reported that land reforms in Vietnam had a positive and significant effect on long-term investment in agriculture and on time devoted to non-farm activities. Examples of lack of employment diversification into non-farm activities in areas where land sales are restricted are found in Sri Lanka (Emran and Shilpi 2011) and Ethiopia (Deininger *et al.* 2003).

Research in India suggests that urbanization is associated with rural nonfarm employment and thereby with rural poverty reduction. In comparison to earlier studies which showed that urban growth had an impact on urban poverty but no discernible impact on rural poverty (Datt and Ravallion 1996), a recent study based on India finds that while rural growth remains vital for rural poverty reduction, urban economic growth has also been good for rural and hence aggregate poverty reduction since 1991 (Datt and Ravallion 2009; Cali and Menon 2012). There are multiple mechanisms that can account for this link. The first and obvious channel is the first-round effects of urban growth inducing migration of poor people in rural areas to urban areas.

A second channel is that rural areas may grow in size over time and become classified as urban. If they had significant concentrations of poor people before reclassification, then rural poverty may decline. There can also be numerous possible second-round effects when urban growth increases the demand for rural goods; leads to growth in marketing, transport and agricultural trade; and leads to remittance incomes from urban to rural areas. Diversification out of agriculture in rural areas may also raise agricultural wages as rural labor markets tighten. The incidence of rural poverty in a district decreases by about 2-3 percent with an increase of 200,000 urban residents in the district (Cali and Menon 2012). This effect is due to reclassification, not migration. The World Bank (2011) reports that growth in per capita consumption in urban areas is associated with growth in rural non-farm employment. As there is also some evidence to indicate that this association is more pronounced in smaller towns than larger cities, promoting poverty reduction in small towns is important for reducing urban poverty and may also help to reduce rural poverty.

Policy makers can leverage non-farm activities that typically connect rural areas to small towns to reduce poverty in both, as well as those created by agglomeration around large cities. For this, they need to focus on the provision of education, connectivity between rural areas, small towns and large cities, electricity provision in rural areas and small towns, and establishment of an efficient land market.

### **Urbanization and delivery of MDG-related services**

Urbanization is usually equated with better access to basic services that enable the poor to have a decent livelihood. Rural-urban differentials are large. In addition, urban areas are not homogenous: some city locations are better served than others. In general, megacities and large cities have the best services, smaller towns have the next best, and slums and rural areas are believed to have the worst access as well as the lowest quality of services. Both slums and small towns contribute to the “urbanization of poverty.” Attention to the small town-large city differentials in urban poverty has shed critical light on the pivotal role that small town poverty is playing. Most of the past and current discussion on poverty in developing countries has been cast in the context of a distinct rural-urban dichotomy: urban poverty is lower than rural poverty.

Since urbanization attracts poor rural migrants and fosters cities in which scale and agglomeration economies offer better jobs and better services, the presumption is that poverty-reducing policies should focus on urban growth in cities. However, if urban poverty is more concentrated in smaller towns, then the singular use of poverty-alleviating measures in cities may be neutralized or even overwhelmed by worsening poverty in smaller towns. The unintended outcome may be significantly lower than expected urban poverty. These differentials can play a pivotal role in determining the coverage, efficiency, and

costs of delivery. The places where the poor live may not necessarily be the least-cost locations for extending coverage of piped water and sanitation, or for building a school or hospital/health clinic.

### Access to primary education affects achievement of prosperity

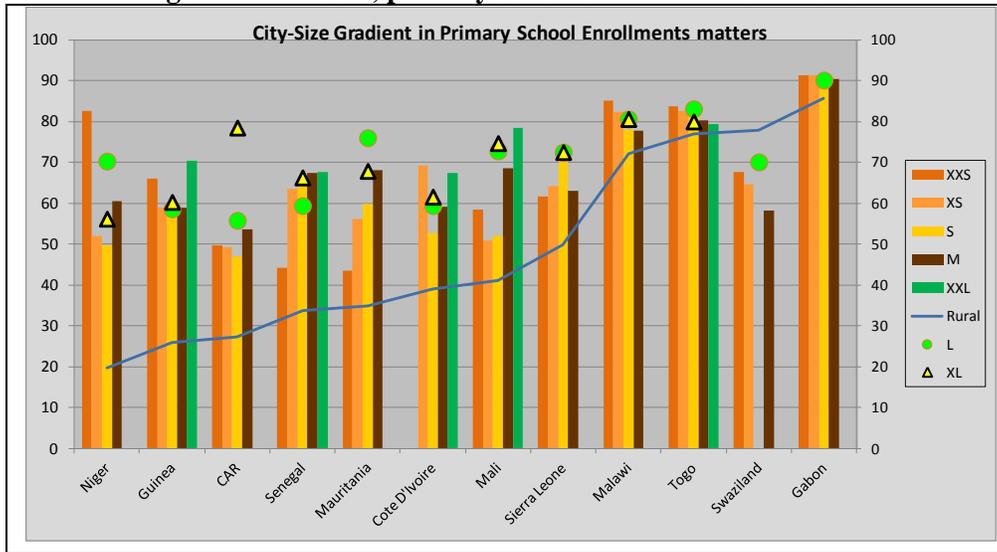
Not all MDG-related services have similar characteristics. Investments in primary education and health care lay the foundations for the human capital endowed in individuals, who can carry the stock with them when they move and add to it if they migrate to places where related secondary and tertiary services are available. Thus, timely investments in basic human capital in rural areas prepare individuals for a city life that offers better paying jobs, and better access to services. In this sense, primary education and health care are portable.

Primary education improves an individual's odds of finding a better paying job, regardless of location. For many rural migrants, the basic education acquired in the village can be the turning point between being prepared for a better paying job and climbing out of poverty upon arrival in a city or remaining in poverty once in the city. Education is by far the most significant determinant of participation in non-farm activities, particularly in high return ones (Lanjouw and Lanjouw 2001 for summary; World Bank 2008; Reardon, Haggblade, Hazell and Reardon 2006; Fox and Sohnesen 2012). Returns to education in non-farm activities are found to increase with education levels. Thus higher education not only improves the probability of landing a non-farm job but also ensures a higher pay-off from such a job.

Early investments in human capital are also necessary to enable further education at the secondary and tertiary levels. Unschooling or poorly schooled rural migrants cannot avail themselves of the opportunities to improve their human capital in the city or take advantage of agglomeration economies. An additional year of schooling raises earnings substantially, reflecting the higher productivity of more educated workers (Psacharopoulos and Patrinos 2004; Montenegro and Patrinos 2012, for the *WDR 2013*). Improving access to primary education in rural areas also has a high payoff as it contributes to raising farm productivity and fostering non-farm employment. Together, nutrition, health, and education combine to form human skills and abilities that have been powerfully linked to productivity growth and poverty reduction in the medium to longer run (Hanushek and Woessmann 2008; Commander and Svejnar 2011). And better health leads directly to higher labor productivity. As such, human capital is a fundamental ingredient for desirable job outcomes (World Bank 2013).

Many developing countries across the regions have made impressive progress in achieving the primary school completion MDG. EAP, ECA, and LAC have either already achieved or are close to achieving the MDG. While they started late, South Asia and SSA are further along in achieving this MDG than most others. More importantly, the differentials in primary school completion rates in rural and urban areas are surprisingly low across these regions (based on data from 46 countries). The *quality* of education, on the other hand, differs more: urban areas have a higher percentage of pupils reaching reading competency than do rural areas. However, given that investments in education at the primary level play a critical role in affecting an individual's lifelong ability to prosper, at least three characteristics related to achievement of this goal are noteworthy: Primary completion rates are lower because primary enrollments are low, especially in rural and smaller towns in SSA (Figure 2.9).

**Figure 2.9: In SSA, primary school enrollment remains low**



Note: XXS (<5,000); XS (5,000-10,000); S (10,000-25,000); M (25,000-50,000); L (50-100,000); XL (100,000 – 1,000,000); XXL (>1,000,000).

Source: Adapted from Lanjouw 2013.

A recent study of 12 SSA countries permits a closer examination of progress toward primary school completion. Recent research also shows that educational attainment needs to be evaluated with more care, as primary completion could be under-reported in the rural areas of low-income countries (Table 2.4). The study calculates an attainment ratio computed for the completion of senior high school, which is itself the result of a two-step process: (i) starting primary school; and (ii) completing primary school for those who started it. Rural-urban ratios estimated at each step of the process help to identify exactly where the main attrition takes place in the education system. Findings from the DHS for a large number of African countries and in South Asia (especially Bangladesh, India, Nepal, and Pakistan) provide interesting results on rural-urban differentials (Nguyen and Wodon 2013 forthcoming).

**Table 2.4: Educational attainment conditional on starting primary education**

	Percentage of children who are starting primary school	Completion of primary among those who started primary school
<b>Bangladesh</b>		
Urban	90	84
Rural	84	75
<b>India</b>		
Urban	92	96
Rural	79	90
<b>Nepal</b>		
Urban	93	93
Rural	83	86
<b>Pakistan</b>		
Urban	82	95
Rural	59	87

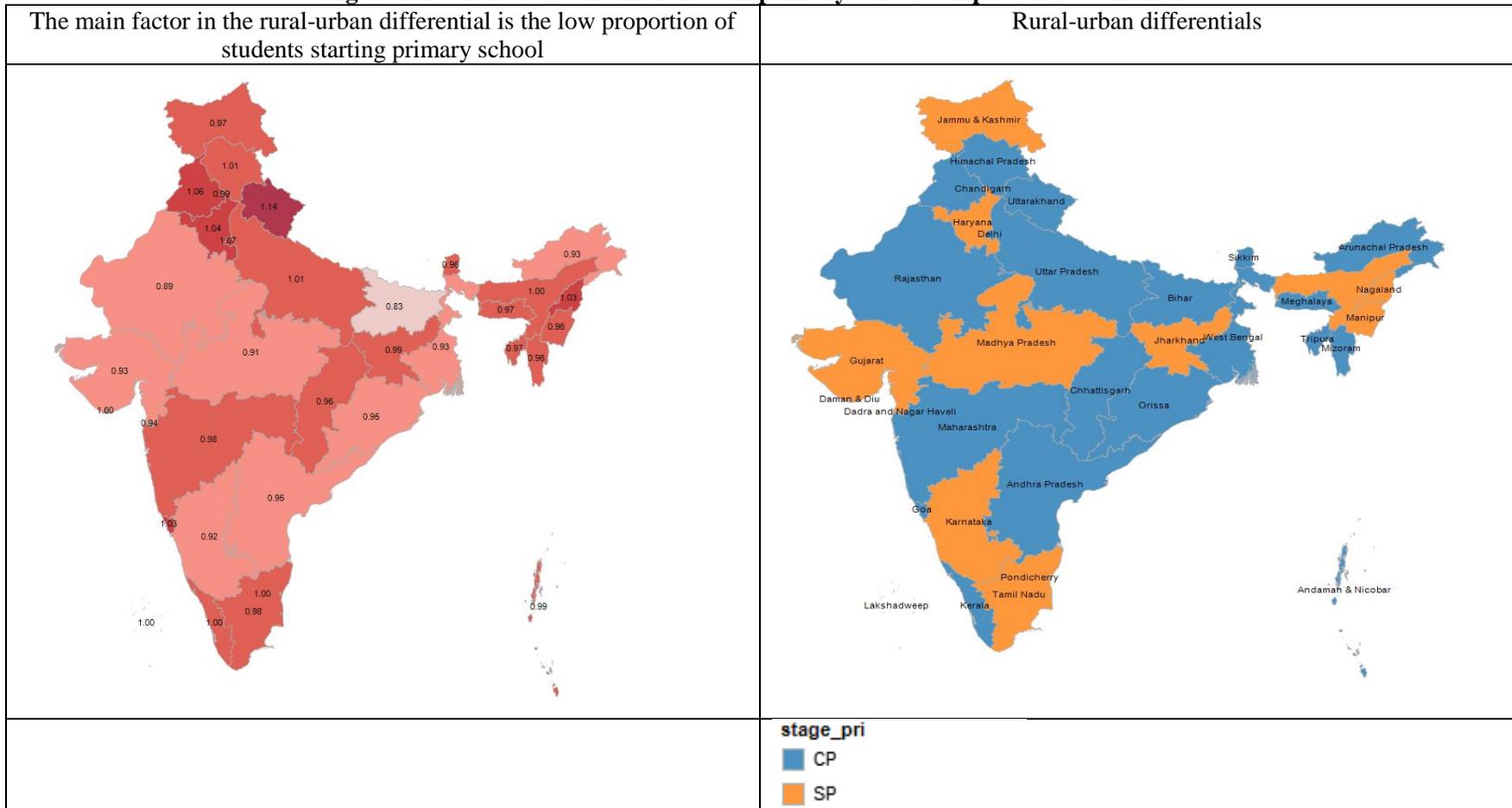
Source: Nguyen and Wodon 2013 forthcoming.

The share of those starting primary education is higher in urban areas and the gap persists at the next level, so that in the end, completion rates in rural areas are less than half those observed in urban areas. As an example, the completion rate in rural Pakistan is 87 percent of the proportion of students who

actually started primary. However, if only 59 percent of the population started school, the actual proportion of rural children completing primary school is 51 percent, not 87 percent. The actual gap in primary completion between rural and urban areas is much larger than the reported completion indicators suggest because they do not incorporate the fact that the student population enrolled is less than 100 percent.

Where exactly in the cohort analysis is the rural-urban gap largest? Which step in attainment leads to the most disparities between urban and rural areas? The findings from India show that the completion of primary school has the most disparities between rural and urban areas. To illustrate this, a map of Indian states shows that in about half of the states, the largest determinant of the gap is fewer students starting primary school in rural areas, while in the other half, completion is the issue (Figure 2.10).

**Figure 2.10: Rural–urban differences in primary school completion rates in India**



Source: Nguyen and Wodon 2013 forthcoming.

## Quality of primary education matters

Progress in primary completion rates does not always translate into superior learning abilities. The prerequisite for poor individuals to benefit from urbanization and escape poverty is participating in the economic opportunities that urban areas offer. Typically, these lie in employment in manufacturing and services sectors, which require basic competencies in reading, writing, and mathematics (simple addition and subtraction). Yet in many cases, these competencies are lacking even in children schooled in cities. In a large majority of the developing countries that took part in the Program for International Student Assessment (PISA) in 2009, at least one-fifth of 15-year-old students were functionally illiterate (did not reach at least level 2 in the PISA reading assessment (World Bank 2013).

Notable rural-urban differentials characterize the *quality* of education imparted to children in poor countries. A comprehensive study in 2007 in 15 SSA countries recorded considerable rural-urban differentials in pupils reaching competency levels in reading and mathematics relative to national scores (Table 2.5; SACMEQ III 2010). The tests were administered to 6<sup>th</sup> graders. Several findings of the study were both noteworthy and worrisome. First, the rural-urban differentials were huge. On average, competency in reading levels 4 – 8 was reached by only 57 percent of the pupils in rural areas compared to 75 percent in urban areas. In Zambia and Malawi, the corresponding figures were less than 25 percent in rural schools and 40 percent in urban schools. Competency in mathematics at even level 4 was discouragingly low: only 18 percent of children in rural schools and 24 percent in urban schools reached this level. Worse, only 1.2 percent of all pupils reached competency in mathematics level 8. Clearly, governments need to pay as much, if not more, attention to the quality of schooling in SSA as they do to completion rates.

**Table 2.5: Pupils' achievement levels in reading and mathematics in SSA, 2007**

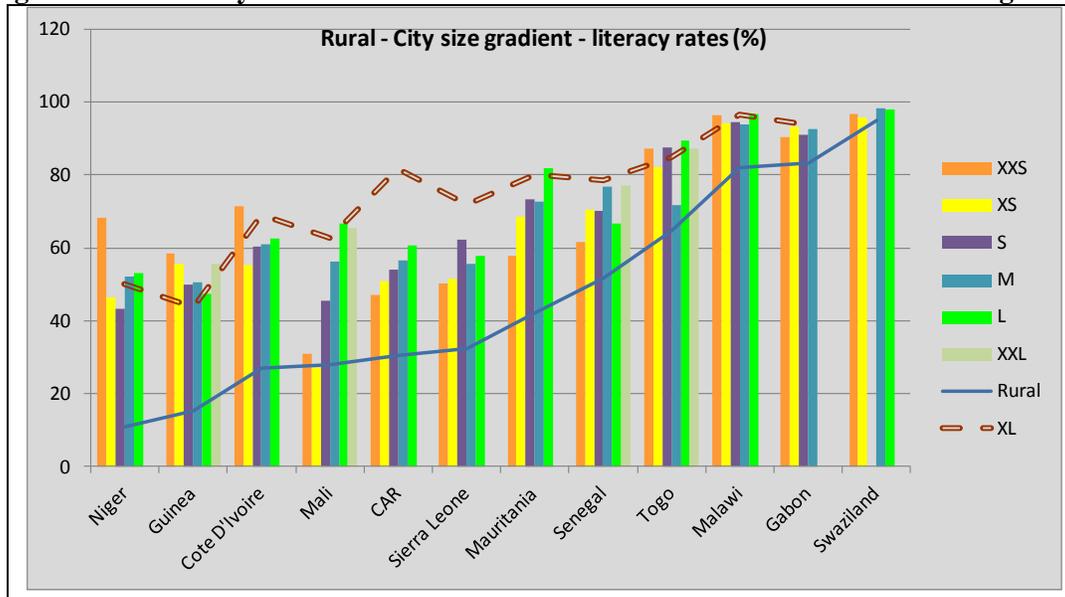
	% of Pupils reaching reading competency level (4-8)				% of Pupils reaching mathematics competency level 4			% of Pupils reaching mathematics competency level 8	Agglomeration Index 2010
	Rural	Urban	U-R differentials	National	Rural	Urban	U-R differentials	National	
Seychelles	78	78	0	78	28	26	-2	1.3	
Malawi	23	38	15	27	5	11	6	0	19%
Mauritius	77	81	4	79	18	18	0	12.2	94%
Mozambique	47	62	15	56	17	23	6	0	24%
Zambia	22	38	16	27	4	10	6	0	31%
Swaziland	91	97	6	93	36	39	3	0	18%
Lesotho	40	63	23	47	10	21	11	0	14%
Tanzania	87	95	8	90	24	28	4	1	23%
Kenya	76	88	12	80	33	30	-3	1.4	37%
Botswana	69	82	13	76	25	29	4	0.4	40%
Uganda	47	74	27	54	15	26	11	0	34%
Namibia	48	82	34	61	7	20	13	0.1	14%
South Africa	31	72	41	52	10	21	11	0.6	52%
Zimbabwe	52	90	38	63	21	27	6	1	31%
<b>Sample average</b>	<b>57</b>	<b>75</b>	<b>18</b>	<b>64</b>	<b>18</b>	<b>24</b>	<b>6</b>	<b>1.2</b>	

Source: SACMEQ III 2010.

Are primary school children in SSA literate? Poor literacy scores in SSA highlight the risk of over-estimating the schooling benefits associated with urban living (Figure 2.11). For example, in Mali,

literacy rates in the smaller towns are as low as those in rural areas. In several countries – Mauritania, CAR, Mali – the differential between larger cities and smaller towns is also huge.

**Figure 2.11: Literacy rates in rural areas and smaller towns are worse than in large cities**



Note: XXS <5,000; XS 5,000-10,000; S 10,000-25,000; M 25,000-50,000; L (50-100,000); XL 100,000 – 1,000,000; XXL >1,000,000.

Source: World Bank 2012.

Children attending primary school in rural areas are often disadvantaged because it is difficult to attract teachers to rural areas. One study finds that about 75 percent of the parents in rural schools complain that the schools do not have enough teachers. This complaint is in addition to one related to teacher absenteeism (Nguyen and Wodon 2013 forthcoming).

When publicly provided primary schooling services are insufficient, private providers can complement education services but affordability is a problem for poor households in South Asia and SSA (Table 2.6). Private providers teach about 23 percent of primary school students, but are concentrated in better served urban areas. Secular and faith-inspired private providers have similar satisfaction rates within urban and rural areas, but higher satisfaction rates than public schools. However, the fees that African households pay to send their children to private secular primary schools are the highest, followed by faith-inspired schools and finally public schools.

**Table 2.6: Market share of public and private schools in Africa (%)**

	Public	Faith-inspired	Private secular
	Market share (15 countries)		
National	77.5	10.2	12.3
Urban	65.9	10.2	24
Rural	82.9	10	7.2
	Satisfaction (6 countries)		
National	56.8	72.8	81.6
Urban	64.4	85.5	86.3
Rural	52.7	61.1	64.1
	Private Cost (US\$, 9 countries)		
National	7	26	84
Urban	17	44	133
Rural	6	19	42

Source: Nguyen and Wodon 2013 forthcoming.

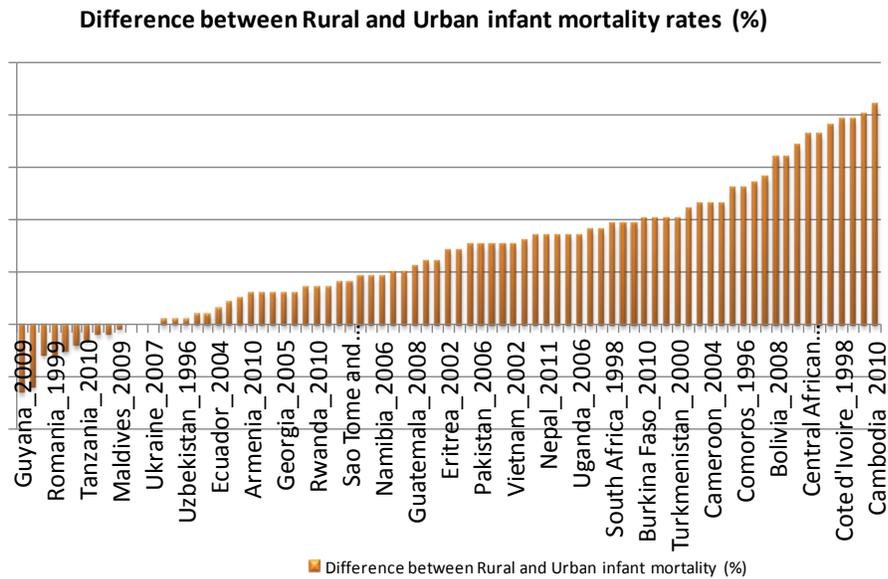
## Rural-urban differentials in health indicators

“Successful development is so intimately related to health – to measures that directly or indirectly help individuals, households or communities avoid or prevent disease, injury and inadequate food intake” (Satterthwaite 2011). Like education, early investments in health care are vital for generations of able-bodied individuals who can use their human capital to improve their livelihoods and take advantages of the opportunities offered by urban living.

The foundations of good health start even before birth. Like basic education, the human capital formation of good health is cumulative and continues to be formed throughout childhood and young adulthood. Of crucial importance are adequate health and nutrition during “the first 1,000 days,” from conception to two years of age (World Bank 2012c). Brain development in this time period affects physical health, learning abilities, and social behavior throughout life (Engle *et al.* 2007; Heckman 2008; Walker *et al.* 2007; Young and Richardson 2007).

Across *all* regions, rural-urban differentials in access to primary health care are significant. Progress in health-related MDGs is closely linked to the scale and quality of provision of sanitation, access to safe water, and primary education. Evidence from DHS surveys for a large number of developing countries indicates that the differentials in infant mortality rates between urban and rural areas are between 8-9 percent in LAC and ECA and between 10-16 percent in MENA, South Asia, and SSA. At 21 percent, EAP has the highest differential. Individual country differences are more informative (Figure 2.12).

**Figure 2.12: Rural-urban differentials in infant mortality rates remain huge**

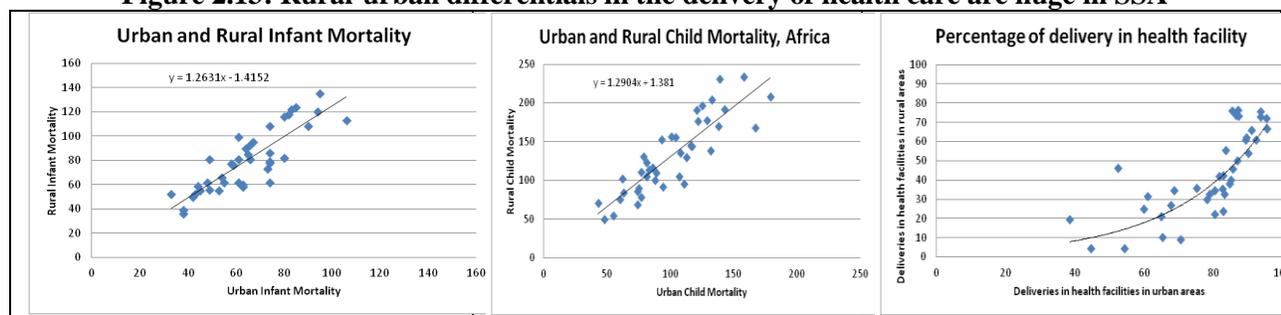


Source: World Bank 2013.

Access to health care for both infants and children under five is equally poor. A study of almost 40 SSA countries based on the DHS indicates that for every 1,000 births, the infant mortality rate is 65 percent in urban areas and 80 percent in rural areas of SSA. The corresponding number of under-5 mortality rate 101 percent in urban areas compared to 132 percent in rural areas.

While many factors underlie the differences in rural and urban mortality rates, including differences in income, consumption, and wealth between urban and rural households, fertility rates and access to safe water, sanitation, and health services play a critical role. The percentage of deliveries in health facilities in urban areas is about 78 percent compared to 43 percent in rural areas in a sample of 28 SSA countries (Figure 2.13). The largest rural-urban differences are in some of the poorest countries (Nguyen and Wodon 2013 forthcoming). Similar patterns are observed for measures of child malnutrition. Worse, many of the relationships between rural and urban measures are essentially linear (i.e., proportional), which implies that the absolute gaps between urban and rural areas tend to be largest in countries with the largest infant and child mortality rates. The average share of stunting in children is 42 percent in rural areas compared to 30 percent in urban areas (Nguyen and Wodon 2013 forthcoming).

**Figure 2.13: Rural-urban differentials in the delivery of health care are huge in SSA**



Source: Nguyen and Wodon 2013 forthcoming.

It is sometimes argued that other dimensions of poverty – health outcomes, for example – tend to be higher in large cities. Analysis of anthropometric outcomes of children across cities of different sizes in Mexico (based on small area estimation methods) indicates a similar gradient: the prevalence of child stunting in Mexico tends to be higher in small towns than in the largest cities (Ferré, Ferreira and Lanjouw 2012).

### Understanding the broader economic consequences of closing health gaps in low-income countries

Most countries are lagging behind in all three health-related MDGs, and the large rural-urban differentials as well as the inter-linkages between the various services affect health outcomes. Given this, it is useful to quantitatively evaluate the broader economic consequences of closing health gaps in low-income countries. In a simulation exercise conducted for this report, the broader economic consequences of closing health gaps in low-income countries were explored by adapting MAMS, a CGE model for country strategy analysis, to address the rural-urban aspects of MDG achievement. The database used was designed to capture characteristics typical of low-income countries, including their MDG outcomes, sectoral shares in value-added, degree of urbanization, and population growth. Annex 1 presents the results of this exercise. The main results indicate if the government can finance increased access to rural health care through a combination of borrowing and greater efficiency in health sector spending, it can considerably reduce rural under five mortality. If the financing is a combination of grants and greater efficiency in health sector spending, government can do more – it can reduce rural under five mortality and contribute to other MDGs including poverty reduction. However, if government has to rely on domestic resources, then the trade-off is lower poverty reduction and less progress in other MDGs. These tradeoffs are especially difficult for governments in low-income countries..

Increasingly, governments are becoming interested in collaborating with the private sector or NGOs to deliver services to the poor. Such partnerships can be instrumental in improving the delivery of health care, especially in South Asia, East Asia Pacific, and Sub-Saharan Africa, where over 90 percent of the poor live (Box 2.2).

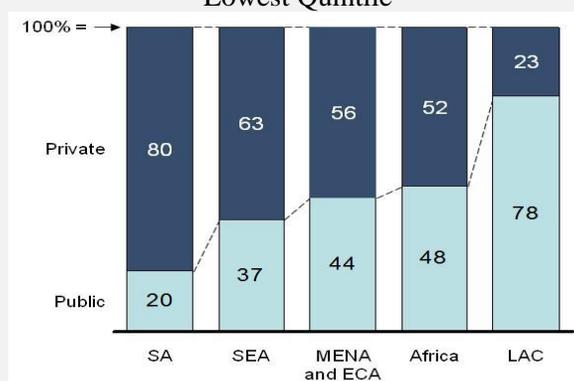
### Box 2.2: Leveraging the Private Sector to Reach the Health-Related MDGs

Over 90 percent of the poor live in South Asia, East Asia Pacific, and Sub-Saharan Africa. In these three regions, the private sector provides at least 50 percent of the health services to the poor.<sup>35</sup> Furthermore, delivery of priority health services by the private sector has been growing rapidly. For example, the proportion of women who delivered children in private facilities increased from 8 percent in 1990 to 22 percent in 2008.<sup>36</sup> Indeed, the private sector already plays and must continue to play an important role in many countries if they are to meet their health-related MDGs.

Some of the innovative mechanisms being pioneered around the world to leverage the private sector are:

- **Smart policies and regulations** with a dual approach to reaching the poor. On one hand, market-wide reforms such as simplifying licensing of health facilities and establishing enforceable patient safety and quality standards are expected to disproportionately benefit the poor. On the other, interventions explicitly target the poor and those private providers that serve them. In Kenya, for example, the World Bank and IFC are helping the National Health Insurance Fund introduce poverty-targeted subsidized coverage. They are also working with the Ministry of Health to introduce the legal and regulatory framework for newly established local governments to contract services from Faith Based Organizations and other NGOs located in the hardest to reach areas of the country.
- **Public-Private Partnerships** that tap the capital, management capacity, and creativity of the private sector to improve public services. In India, IFC helped the State of Meghalaya design an innovative insurance scheme whereby the government, a private sector insurer, and hundreds of empanelled public and private healthcare providers cooperated in a large-scale partnership to enhance financial protection and access to quality health care for the population of one of the lowest income states in the country.
- **Capital finance** that fuels expansion of access to quality health services and products from the private sector. IFC is investing in and advising health care companies seeking to expand access to quality health services and products to those at the “bottom of the pyramid” (BoP).<sup>37</sup> In Africa, IFC helped establish an innovative private equity fund that not only focuses on health but is also explicitly incentivized to finance companies that serve the BoP. One such company is the Nairobi Women’s Hospital. An independent assessment shows that a little over 60 percent of its patients are in the BoP. In India, IFC investee Apollo Hospitals is seeking to expand its top quality services to smaller cities and rural areas.

**Percent seeking care in private versus public facilities by region**  
Lowest Quintile



Source: DHS Surveys.<sup>38</sup>

<sup>35</sup> [www.ps4h.org/globalhealthdata](http://www.ps4h.org/globalhealthdata)

<sup>36</sup> Karen Grepin, - <http://ps4h.org/ihea2011>

<sup>37</sup> BoP: annual household income of less than US\$3000; bottom of the BoP US\$1000 on PPP basis.

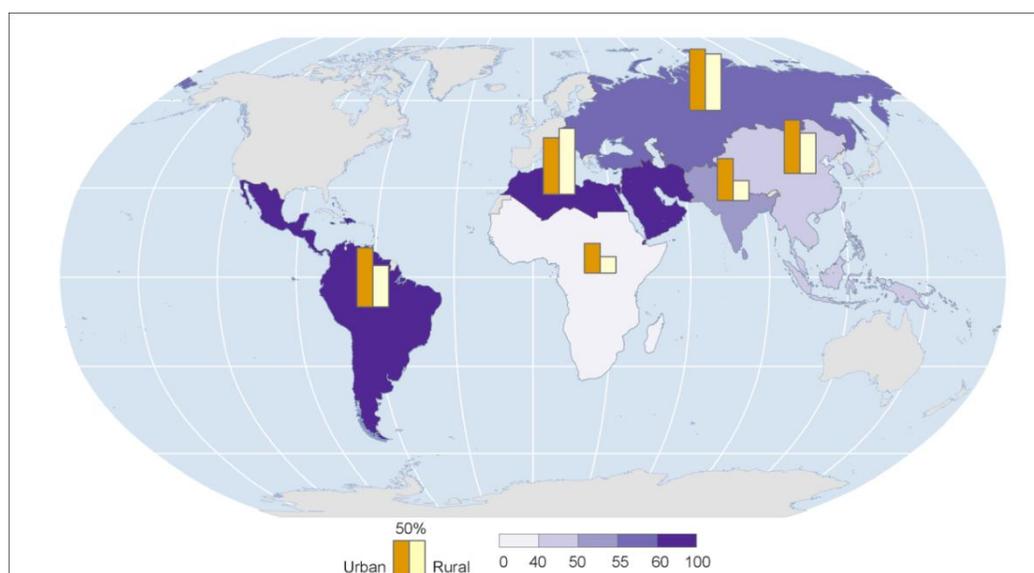
<sup>38</sup> [www.ps4h.org/globalhealthdata](http://www.ps4h.org/globalhealthdata)

### Affordable access to sanitation and water – infrastructure needs scale economies

In comparison to basic education and health care whose benefits are embedded in an individual’s human capital, infrastructure needed to increase access to safe water and sanitation must be provided at a fixed spatial location. New or old connections in a rural area cannot be moved costlessly to urban areas. The initial fixed costs of establishing these services are high; routine maintenance is also costly. They are also most cost-effective when delivered through networks, i.e., water pipes and sewers. Sparsely populated rural areas are unable to benefit from scale economies that reduce the unit costs of network infrastructure services such as water and sanitation because they do not have the necessary population density. Because of less economies of scale, residents in less agglomerated areas (rural population, very small towns and peri-urban, less dense areas) often get a lower level of service (individual solutions for sanitation, or nearby standpipes). If migration of the rural poor to urban areas is high, the provision of these services may be more affordable in the urban areas to which the poor would migrate in search of jobs and where the population density would give rise to scale economies.

The best illustrations of rural-urban disparities in the delivery of MDG-related infrastructure services are in South Asia and SSA (Figure 2.14). Evidently, the high incidence of extreme poverty in these regions extends equally to non-income markers of poverty. In SSA and South Asia, where about 20-40 percent of the population resides in urban areas, access to sanitation in rural areas is significantly lower or at best close to the levels available to urban residents. Sri Lanka and Mauritius are prime examples. In comparison, in LAC, MENA, and EAP, which have a higher agglomeration index, rural residents’ access to sanitation is higher in both urban and rural areas and the rural-urban differentials are much smaller.

**Figure 2.14: Within countries, access to sanitation is better in urban areas even in the most urbanized countries (share of population with access (%))**

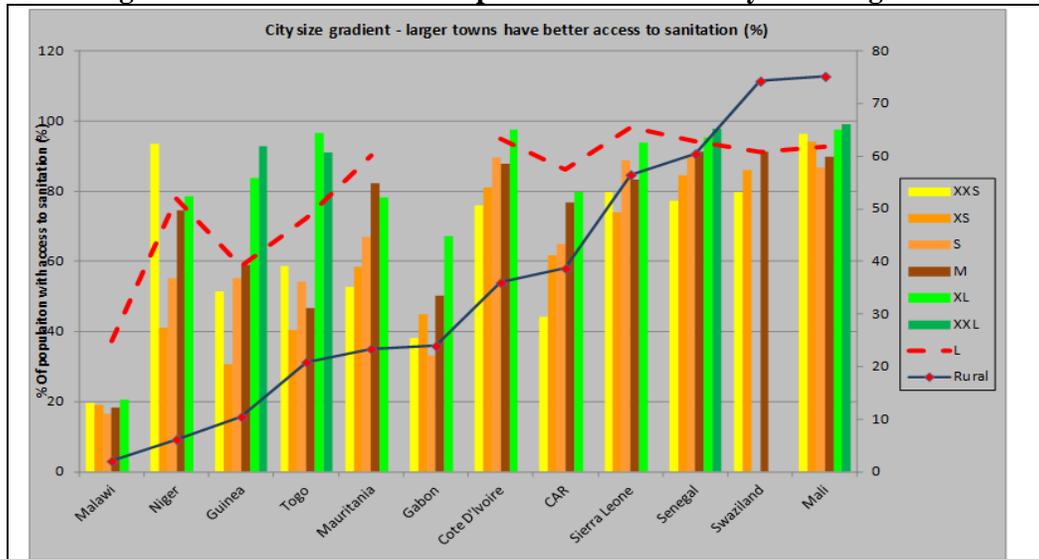


Source: World Bank Development Indicators.

To the extent that infrastructure availability acts as a determinant of urban growth and poverty reduction, the imbalance of service availability could help explain lower welfare outcomes in smaller towns. In at least 12 countries shown in Figure 2.15, the differences in access to sanitation between the largest cities and smaller towns are as stark as those between urban areas as a whole and rural areas. In Mali, Niger,

and Mauritania, access to sanitation in the smallest towns is only half of that in larger cities. The statistics in the CAR and Sierra Leone suggest that urban residents in these places have no access. Niger, Gabon, Malawi, and Swaziland can celebrate the outcomes – people in smaller towns can turn on the tap and expect safe water to flow, just like residents in larger towns.

**Figure 2.15: Small towns have poorer service delivery than large cities**

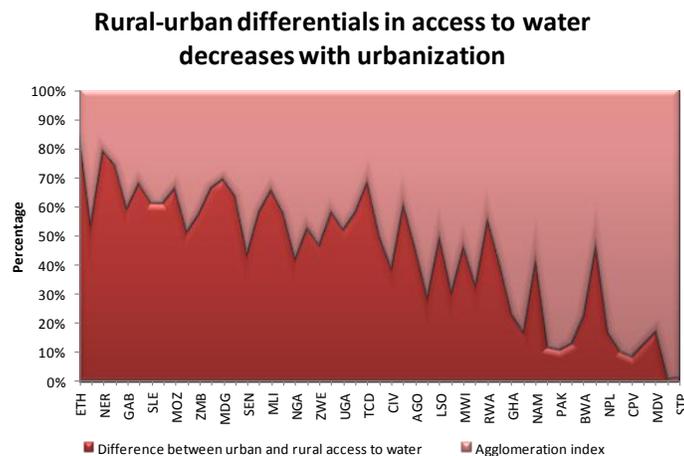


Note: XXS <5,000; XS 5,000-10,000; S 10,000-25,000; M 25,000-50,000; L 50-100,000; XL 100,000 – 1,000,000; XXL >1,000,000.

Source: World Bank 2011.

South Asia and SSA offer modestly better access to safe drinking water in rural and urban areas, though rural-urban differentials remain significant (Figure 2.16). In general, the rural-urban differentials in access to water are positively related with the level of urbanization in most regions. The largest differentials (about 70 percent or higher) are in Ethiopia, Niger, Gambia, and Sierra Leone, which are mostly rural.

**Figure 2.16: Access to safe water is nearly equal in rural and urban areas of SSA and South Asia**



Source: World Bank 2012a.

How much has access to basic MDG-related infrastructure services improved in Africa's urban and rural areas and how much remains to be done? The Demographic Health Surveys for Africa indicate that

between 1990 and 2005, in part due to population growth, access rates within urban areas have either declined or remained stable, while those in rural areas have not changed much or have increased, suggesting that migration has contributed more to the higher access rates than service delivery improvements (Table 2.7). It is unlikely that the situation has changed dramatically since 2005 (Banerjee, Wodon and Foster 2010; Estache and Wodon 2013). In 2010, 96 percent of the urban population in developing countries had access to safe drinking water compared to 81 percent of the rural population. However, in LAC, coverage improved in both urban and rural areas alongside continued urbanization because, in general, governments have been able to cope with this shift in water and sanitation demand.

**Table 2.7: Access to basic infrastructure services in SSA, 1990–2005 ( %)**

	Piped Water			Flush Toilet		
	1990-1995	1996-2000	2000-2005	1990-1995	1996-2000	2000-2005
<b>National</b>	18	17	17	9	9	10
<b>Urban</b>	50	43	39	32	29	27
<b>Rural</b>	4	4	4	1	1	2

*Source:* Banerjee, Wodon and Foster 2010 (see also Estache and Wodon 2013).

Apart from creating better paying jobs, cities also make, through their density, public services more accessible. For example, on average it costs US\$0.70 to US\$0.80 per m<sup>3</sup> to provide piped water in urban areas versus US\$2 in sparsely populated areas. The poor often pay the highest price for the water they consume while having the lowest consumption levels. For example, in Niger, the average price per m<sup>3</sup> of water is CFAF 182 for piped water from a network, CFAF 534 from a public fountain, and CFAF 926 from a vendor (Bardasi and Wodon 2008). More than 55 percent of households did not have access to piped water in their dwelling. Having a private connection was strongly correlated with wealth – among the poorest 20 percent of households, none had a private connection, while 65 percent of households in the top quintile were connected. And poor access to basic infrastructure disproportionately affects rural women, as they perform most of the domestic chores and often walk long distances to reach clean water. In several rural and small towns in SSA, where network connections are often not economically viable, public private partnerships have been designed to leverage innovative means for delivering safe water (Box 2.3).

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**Box 2.3: Water in Africa: Sustainable PPPs in Rural and Small Towns - Strong Public Sector Leadership is Key**

**Public-Private Partnerships (PPPs) in non-traditional markets.** Non-traditional markets, such as those in sparsely populated and dispersed settlements, present a challenge to making private sector participation a commercially viable proposition because of economies of scale and affordability issues. The experiences in Cambodia, Mozambique, Mali, Rwanda, Senegal, the Philippines, and Uganda have shown, however, that given the right allocation of risks, interest can be generated in the private sector to venture into these waters. In many African countries, the private sector's role is mostly confined to operating rural water supply schemes, generally small piped water schemes serving households through a combination of private connections and standpipes. In India, the private sector is involved in higher value-added services, such as processing and disposal of solid waste. Success comes not just by helping develop PPP arrangements but also by strengthening the enabling legal, regulatory, financial, and institutional environment.

**Rural growth centers and small towns dominate the challenge of water service delivery in Sub-Saharan Africa.** Today, 2.6 billion people live without access to improved sanitation. Of these, 75 percent live in rural communities. Sub-Saharan Africa's settlements will be dominated by rural growth centers and small towns where populations range from 1,000 to 50,000 inhabitants. This is Africa's biggest challenge for network water service provision given the generally lower population densities over larger land areas and lower incomes.

**Private participation as a vehicle for public policy implementation.** In developing countries, local private sector companies and entrepreneurs have worked as partners to deliver water supply services in rural growth centers and small towns. In Sub-Saharan Africa, a number of governments have explicit policies for the delegation of water supply services to private operators, as in Benin, Burkina Faso, Mali, Mauritania, Mozambique, Niger, Rwanda, Senegal, and Uganda. Affermage, lease, and management contracts are the most common types of contract today, whereby operators take commercial and operational responsibility, including for small repairs.

**Key lessons from the field: actors of financial viability suggest the need to lower the cost of services in rural areas to drive consumption.** Evidence suggests that a growing number of privately operated schemes are just able to achieve operating cost recovery, with a few making comfortable margins. What separates financial winners and losers? Analysis in Uganda found that the number of active connections was a strong positive determinant of financial cost recovery. More active connections translate to higher volumes of water sold, given that consumption tends to be higher from private house connections than standpipes. This observation captures the common issues across countries: the price of water and connections, rates of consumption, and economies of scale. In rural growth centers outside of small towns, the cost of service tends to be higher than in urban areas. Lowering the cost of service requires approaches that are usually not easy to coordinate or navigate politically and hence, they are typically not undertaken. These include: (i) subsidizing the densification of standpipes to bring them closer to household settlements or subsidizing the cost of house connections; and (ii) clustering schemes across different political/administrative boundaries to be managed by a single operator.

**Holding local institutions accountable matters in the success of the partnership and in rehabilitation.** Private sector participation in Africa is often an accompaniment to political devolution, which saw the responsibility for water services decentralized to the local level. This is the case in Benin, Burkina Faso, Mali, and Uganda. The role of local governments as the focal point between the state, consumers, and the private sector is critical. Often, however, transfer of authority for water services is incomplete and not well thought out. Uganda is unique as it has set up a dedicated and autonomous local body that represents the public sector in water services delivery. In contrast, most West African countries, such as Benin and Burkina Faso, expect the local communes (mayor) to take on oversight for water services as an additional mandate.

*Source:* Water and Sanitation Program (<http://www.wsp.org/topics>).

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Poor people are willing to move to gain access to basic services. Poor people already pay for access to services in rural areas but they are also willing to pay for them in urban areas. Their desire to access better education and health services to enrich their families' human capital and future income is a motivation for moving to urban areas. Lall, Timmins and Yu (2009) combined a rich data set of public services at the municipality level with individual records from four decades of Brazilian census data to evaluate the relative importance of wage differences and public services in migrants' decisions to move. Their findings showed a clear distinction in preferences according to income level: for relatively well-off people, basic public services were not important in the decision to move, but for the poor, differences in access to basic public services did matter. In fact, Brazilian minimum wage workers earning an average R\$7 per hour (about US\$2.30 in February 2008), for example, were willing to pay R\$420 a year to have access to better health services, R\$87 for a better water supply, and R\$42 for electricity.

## Urbanization, congestion, and slums

Typically, slums emerge in cities when the demand for services outpaces supply and grow due to natural increases in the urban population or to rural-urban migration. Slums can be a transient home for some migrants and a permanent one for others.

There is no technical definition of a slum, but several indicators are associated with slums: “a group of individuals living under the same roof in an urban area with at least one of the following four basic shelter deprivations: lack of access to improved water supply; lack of access to improved sanitation; overcrowding (three or more persons per room); and dwellings made of nondurable material” (UN Habitat Expert Group Meeting 2002). A fifth indicator is insecurity of tenure, but due to insufficient data, this dimension is not formally included in estimates of slums. In April 2011, however the UN Habitat Governing Council adopted a resolution to improve the measurement of tenure security and to generate globally comparable estimates. Observations using this method are being implemented in 25 cities around the world.<sup>39</sup>

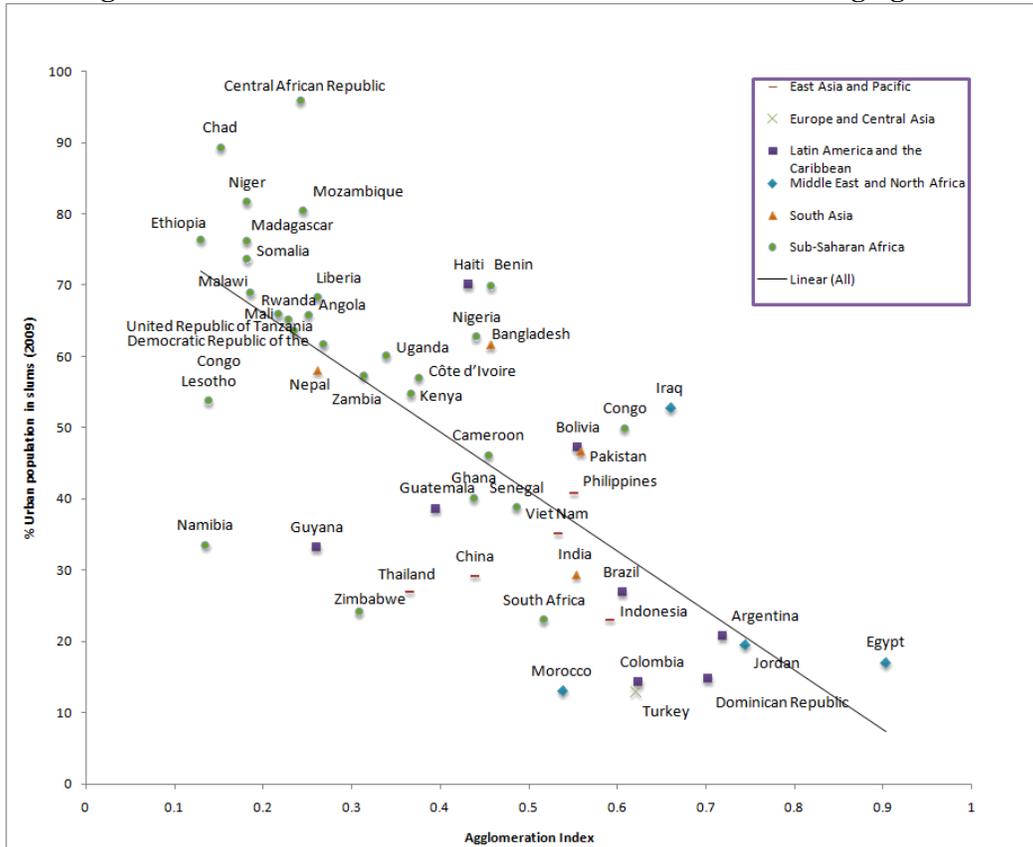
In developing countries, all five indicators often occur together and deprivation occurs in extremes. Given that the two poorest regions – SSA and South Asia – have the worst record on access to safe water and sanitation, it is no surprise that they also house a large proportion of their urban population in slums (Figure 2.17). Poorly functioning land and housing markets, lack of urban planning, and exclusionary attitudes towards the urban poor are the main reasons why the urban poor are forced to reside in low quality housing on insecure public and private land with few or no basic services (Baker 2007). Further,

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<sup>39</sup> This methodology aims to generate estimates based on micro and macro indicators of tenure insecurity. Micro indicators are based on household level data were collected through Urban Inequities Surveys that were added onto existing household surveys. Macro level data have been generated through qualitative analyses of existing policies, legislative provisions, and their level of implementation, which resulted in the creation of the Legal and Institutional Framework Index (LIFI). This multi-level methodology was piloted in Sao Paulo, Brazil, and highlighted important dimensions of tenure insecurity based on housing documentation and risk of eviction. This study concluded that the tenure security level for the citizens of Sao Paulo could be described as medium at best, a result that differs from other estimates that have placed the urban poor in Sao Paulo as having a high level of tenure security. Although the majority of Sao Paulo households enjoy a legal or legitimate status in their relation to land, the legislative and institutional framework for Brazil and Sao Paulo do not provide an enabling legislative framework needed to see positive results with respect to tenure security for urban poor. Results from surveys being conducted globally are likely to provide a much needed understanding of the extent of tenure insecurity faced by the urban poor, which in turn might lead to revised estimates for the number of slum dwellers globally.

insecurity of tenure takes on complex forms in situations where slum populations represent a mix of owners, squatters, and renters.

**Figure 2.17: Slums decline as countries become better at managing them**



Source: (1) Slum data from United Nations Human Settlements Programme (UN-Habitat) Global Urban Indicators Database 2012, which is based on computations from country household data using the four dimensions of slums (improved water, improved sanitation, durable housing and sufficient living area). (2) Agglomeration Index 2010 World Bank.

Slum settlements may have differing degrees of marginalization depending on the recognition of their status by the government. Slums may actually serve the urban poor by offering low-cost housing and potential proximity to work. Slum settlements can also be the basis for self-employment and operation of small home-based businesses.

### Markers of slums

Lack of basic services in cities is often tied to insecure tenure. According to the UN’s *MDG Report 2012* (UN 2012), slum evictions without due legal process are the most visible violation of housing rights confronted by urban poor. There has been a significant rise in slum evictions since 2000. For example, in 2003/04 in Jakarta, as part of an effort to clear various areas of informal occupation, over 100,000 people were either evicted or threatened with eviction; in Beijing, China, an estimated 300,000 people lost their homes as a result of preparations for the 2008 Olympic Games (Du Plessis 2005).

While in the short run slum and informal settlements may provide an entry point into cities, they are likely to have negative impacts on the conditions of the urban poor in the medium and long term. A lack of government intention to provide basic services in slum settlements does not necessarily deter urban

poor and rural migrants for whom slums are the only entry point into urban areas. It does, however, negatively impact their economic situation if they have no choice but to rely on private and informal providers for provision of basic services at higher cost than those provided by the government to other strata of the society (see Box 2.4). Eviction from slums can also affect the livelihood of the residents drastically in several ways: by spatially displacing them from the proximity of their livelihoods, creating higher transportation costs, and by destroying the site of their livelihood since slums are also sites of economic production for small business enterprises (Mehra *et al.* 2012; Du Plessis 2005). Given the lack of access to insurance or secure savings, such losses can create dire economic conditions for the urban poor. Slum dwellers often cope with these problems by discontinuing the education of children, especially girls.

More significantly, the lack of legal recognition of slum settlements translates into poor access to basic services, especially water and sanitation. For example, more than 50 percent of the slum population in South Asia and 40 percent in SSA lack access to sanitation services (UN-Habitat 2011). In the slums of Nairobi, Kenya, there is one toilet for every 500 people on average. There are also some encouraging though rare examples, such as the one related to an NGO-led initiative to redress the lack of toilets in Agra, India (Box 2.6). Governments are reluctant to provide basic services to slum settlements with insecure tenure. They mistakenly view such actions as encouraging further urban poor settlement on unoccupied lands and as an invitation to rural migrants to migrate to cities in expectation of better services (Durand-Lasserve 2006). According to the *World Population Policies Report (2011 Revision)*, in 1976, 44 percent of developing countries reported having implemented policies to restrict or retard rural-urban migration; by 2011, that proportion had increased to 72 percent. Further, the inability of migrants to prove urban residence via water or electricity bills or formal rental leases in slums, along with their informal employment, makes their situation even more precarious. In some countries, proof of urban residence is needed to access basic services. A qualitative study undertaken by the American University of Central Asia in Bishkek, Kyrgyzstan, found that without proof of urban registration status, rural migrants are denied treatment at health services and many no longer approach health services knowing that they will not be treated (Nasritdinov 2011).

### **Box 2.4: Costs of Coping with Lack of Water Service Provision**

In Bangladesh, in the absence of state provided services, a parallel network of service providers known as *mastaans* provide the needed services for high fees, with patronage from politicians and law enforcement agencies (World Bank 2007). Based on interviews with government agencies and NGOs, a World Bank (2007) report noted that the *mastaans* exploit slum residents not only by demanding high rates for the provision of basic services but also by using physical force and threats of eviction when payoffs are not made.

Such instances are not limited to Bangladesh. Water sold at water kiosks in informal settlements in Eldoret, Kenya, costs more than five times what residents in the formal urban areas of Eldoret pay the municipal council for water (Kimani-Murage and Ngindu 2007). Karuiki and Schwartz (2005) analyzed data from 47 countries (93 locations) and found that the average water prices charged by private vendors compared to the formal network were 4.5 times higher for point sources (ranging from a simple connection to a standpost/kiosk and tap to a borehole with tank, pipe and tap) that are most commonly found in peri-urban or unplanned settlements with unclear tenure.

These higher costs of access to water associated with the use of informal providers not only increase the non-consumption expenditures of slum dwelling households but may also increase costs related to ill health. In Indonesia, the use of low-priced drinking water from informal providers by slum families was associated with considerably higher infant and under-5 mortality as well as child morbidity (Semba *et al.* 2009). The lack of safe water provision in urban slums has far reaching implications and threatens the progress on MDGs related to poverty eradication and child health.

Substandard housing or illegal and inadequate building structures are another housing-related marker of slums. Overcrowding and high density worsen service delivery when one tap/toilet supplied to a dwelling has to be shared by many. Overcrowding is associated with a low space per person, high occupancy rates, cohabitation by different families, and a high number of single-room units. Many slum dwelling units have five or more persons sharing one room used for cooking, sleeping, and living. Bangkok requires at least 15 dwelling units per rai (1,600 square meters).

Slums are characterized by unhealthy living conditions and hazardous locations that result from a lack of basic services, manifested by visible, open sewers, a lack of pathways, uncontrolled dumping of waste, and polluted environments. Houses may be built in hazardous locations or on land unsuitable for settlement, such as floodplains, in proximity to industrial plants with toxic emissions or waste disposal sites, or on areas subject to landslide. The layout of the settlement may be hazardous because of a lack of access ways and high densities of dilapidated structures.

Slums and child mortality go hand in hand. A slum household that suffers from a disease such as diarrhea can be one or two times more at risk when it is extremely deprived than when it is affected by only one deprivation. For example, in Ouagadougou, the capital of Burkina Faso, the proportion of children with diarrhea in slum areas is 20 percent, whereas those children living with three shelter deprivations are two times more exposed (37 percent) and those with four shelter deprivations are 2.5 times more at risk. Likewise in Harare, the capital of Zimbabwe, children in slum households suffering from two shelter deprivations are five times more exposed to diarrhea than children in slum households with only one shelter deprivation (UN-Habitat 2008).

A Nairobi Urban Health and Demographic Surveillance Site (NUHDSS) study indicates that slum children bear the biggest burden of poor environmental sanitation and housing conditions and poor quality health services. Autopsy data from the NUHDSS have shown that diarrhea and pneumonia are the leading causes of death among children under five years old and that the mortality burden among these children is four times higher than in the rest of the population (Kyobutungi *et al.* 2008). These mortality levels are not surprising given that children in slums have exceptionally low levels of vaccination (44 percent are fully immunized) (Mutua and Kimani-Murage 2011). The children in NUHDSS slums were also found to have exceptionally high levels of malnutrition and a high prevalence of infectious diseases in the midst of poor access to curative health care (Ndugwa and Zulu 2008).

Women's disproportionate burden of improper sanitation has crucial implications for other MDGs. In overcrowded and underserved urban slums, the lack of basic sanitation and safe water is an acute problem for women and girls. Many wait until dark to relieve themselves, often confronting harassment and even sexual assault when defecating in public. As women carry a heavier burden of household chores (including cleaning, washing, and caring for children), the lack of water and sanitation provision in slums affects them disproportionately more than men.

A recent study of 5,033 migrant women living in makeshift slum settlements in India found a strong statistically significant relationship between women's diseases and lack access to basic sanitation (Singh *et al.* 2011). A lack of gender-balanced approaches to sanitation also has significant impact on MDGs related to the education of adolescent girls. Poor sanitation is a leading determinant of adolescent girl dropouts (MoE Kenya 2011; APHRC 2010; FAWE 2006; Obonyo 2003). A UNICEF study in urban Bangladesh found that a simple school sanitation intervention to provide separate facilities for boys and girls helped boost girls' school attendance 11 percent per year, on average, from 1992 to 1999 (UNICEF 2003a). Similar results were found in Mozambique (UNICEF 2003b).

Slums often surface on the periphery of a city, but the problems are the same as those in the city center. As Satterwaithe (2007) observes, settlements are formed on the urban periphery of many cities (including superstar cities like Buenos Aires, Delhi, Manila, Mumbai, Phnom Penh, Santiago, and Seoul) when evicted inhabitants were forced out to these areas by local government slum clearance schemes. The social and environmental consequences include the segregation of low-income groups in the worst located and often most dangerous areas, a lack of access to water, sanitation, health services, and educational facilities, and other environmental risks. This is particularly the case for recent rural-urban migrants who may not be able to afford rentals within a slum, and have to squat on sites that may not be fit for habitation. Unfortunately, these sites are also prone to significant environmental risks.

Heath, Parker and Weatherhead (2012) utilized Rapid Climate Adaptation Assessment (RCAA) to assess how changes to climate interact with existing vulnerabilities in peri-urban and informal areas in a manner that is likely to affect safe water and sanitation supply for the urban poor. The model was tested in Lusaka (Zambia), Naivasha (Kenya), and Antananarivo (Madagascar); in the 11 communities studied, eight were found to be vulnerable to flooding and four to water shortages, with especially severe negative effects for the peripheral sites prone to flooding. For example, in the peri-urban slum settlement of Kanyama on the outskirts of Lusaka, the 2009/10 flood lasted for three months, causing water kiosks and buildings to collapse, contaminating water supplies (particularly the shallow wells used in the areas unserved by the kiosks), and affecting livelihoods, education, and health. Satterwaithe (2007) argues that in several cities,

extreme overcrowding in informal settlements (including the unserviced ones on urban peripheries) is seen as a result of serious housing shortages and acute shortages of infrastructure and services in particular areas. Yet large amounts of land in cities are often left vacant or only partially developed; planning for low-income housing with proper basic services and infrastructure could result in lower costs than those incurred in upgrading existing dense settlements, resettling slum dwellers, and undertaking slum clearance projects.

In a few countries, disappointed with government's lack of interest in their plight slum dwellers are taking the initiative to make their voice heard in the sphere of policymaking. Two examples are insightful and encouraging. In Agra, India, a community-driven, NGO-facilitated, and local government-supported initiative has made toilets an entry point for catalyzing housing, slum, and city development (Box 2.6). In Uganda, in a slum dweller community of Uganda where over 60 percent of the country's urban population lives, the purported benefits of urban agglomeration are not being felt. Rather than waiting passively for better service provision, Uganda's slum dwellers have adopted a proactive strategy that is, given high levels of unemployment and lingering low quality of services even where access is improving. Rather than waiting passively for better service provision, Uganda's slum dwellers have adopted a proactive strategy that is harnessing the potential of collective action to drive a shared agenda for better service delivery in slums (Box 2.5).

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**Box 2.5: Agglomeration of Collective Capacity among Uganda’s Slum Dweller Communities**

In the slum dweller communities of Uganda – where over 60 percent of the country’s urban population lives – the purported benefits of urban agglomeration are not being felt, given high levels of unemployment and lingering low quality of services even where access is improving. Rather than waiting passively for better service provision, Uganda’s slum dwellers have adopted a proactive strategy that is harnessing the potential of collective action to drive a shared agenda for better service delivery in slums. This strategy has evolved in the form of clusters of community saving groups that came together in 2002 to form the National Slum Dwellers Federation of Uganda (NSDFU). The NSDFU is comprised of almost 500 savings groups, with 62 networks encompassing about 38,000 saving group members. Savings are used to bring people together, to build their capacity to act as a collective, and to build organizational capacity and trust. When savings groups begin, they often focus solely on livelihood issues and income generation. But with time and greater exposure to federation rituals such as enumeration and peer-to-peer exchange, communities formulate an urban agenda that looks beyond group members to collaborate with other groups. This is when benefits to service delivery begin to accrue as part of a collective upgrading agenda.

The spatial proximity of urban savings groups allows for the agglomeration of collective capacity necessary to create a critical mass of urban poor to hold public officials accountable, to collaborate with municipalities and leverage their savings, and to bring about change. This critical mass is required to make community participation more than a platitude and aid more effective, and it is uniquely possible in the urban setting. The positive externalities of the agglomeration of collective capacity in communities of the urban poor in Uganda are not hard to see. NSDFU has been active in Arua, Jinja, Mbale, Mbarara, Kabale, and Kampala. It is creating new models of community-driven partnerships with municipal councils; implementing creative financing solutions combining community savings and municipal contributions; negotiating secure tenure and identity documentation for slum dwellers; and building community capacity by training members to carry out safe self-construction. Over the last 10 years, NSDFU members have successfully: constructed, upgraded, and maintained sanitation units within several slums; extended water supply (with an ongoing project in partnership with Arua Municipal Council); improved drainage throughout the country’s slums; and even secured land from local governments to build planned low-cost housing (e.g., 7.6 acres for the Kawama Housing Project in Jinja Municipality).

These organized communities have also improved: municipal/city governance, by sharing the information required for citizens to create accountability; city planning, by generating statistics on slum populations; and the urban environment, by upholding their responsibilities to keep cities clean and maintain public services. As the federation grows, it becomes easier to negotiate with the government and increase the efficiency of implementing its projects. The increasing returns to scale for the agglomeration of collective capacity are not limited to Uganda, since the NSDFU is one of 33 federations in the Shack/Slum Dwellers International network, which facilitates cross-country collaboration and knowledge exchange among the federations.

*Source:* Skye Dobson, Uganda Program Officer, Slum Dwellers International.

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**Box 2.6: Catalyzing Citywide Development through Toilet Design in the Slums of Agra, India**

The city of Agra is making news with a community-driven, NGO-facilitated, and local government-supported initiative that has made toilets an entry point for catalyzing housing, slum, and city development. In the slums of Agra, the user-toilet ratio is as high as one seat for every 345 to 1,000 users. Personal toilets are a luxury for several reasons. Poor families with little savings or access to affordable formal credit are unable to invest in building a toilet (the initial investment is estimated to be up to six months of a poor household's earnings in Agra). Lack of space in small and temporary slum structures makes it impossible to construct a toilet using conventional technology. Plus, there is a lack of technical knowhow to make the connection to a sewer line (usually far away from a slum) or to a safe underground septic tank connected to a conveyance system. Women, who are disproportionately affected by the lack of toilets, have little influence on spending decisions to construct a toilet. Finally, the biggest constraint is the insecure tenure of slums. Local bodies are reluctant to permit construction of permanent structures for the fear of legitimizing stay and raising entitlement issues.

The Centre for Urban and Regional Excellence (CURE), an Indian NGO, has approached the lack of private toilets for slum dwellers using a four-cornered strategy by: (i) enabling women to be the decision makers; (ii) creating access to credit and technical knowhow; (iii) designing, improving, customizing, and stabilizing the technology with last mile connections; and (iv) enhancing local capacities to address organizational, governance, and scaling-up restraints. Toilet Savings Groups of CURE enable women to save and set aside money for construction. The balance comes from a Community Credit Fund, repaid in small installments, and the money revolves to other toilet-less families. While the plumbing, pan, and collection/conveyance system is mandatory, women can choose to make the walls, roof, doors, etc. from less permanent material to save costs. State permissions and reformed local bylaws also encourage families to invest in toilets.

Toilet designs were customized to suit the slum environment; e.g., septic tanks were retrofitted and strengthened in partnership with a local manufacturer who was also trained to install the full toilet on a turnkey basis for long-term sustainability. Surface drains were improved to convey septic tank overflows to the city drain, where the city's first Decentralized Waste Water Treatment System (DEWAT) was built with support from international donors and Agra Municipal Corporation. To simultaneously ensure environmental safety and convey toilet waste away from homes, cluster septic tanks were designed below neighborhood parks and linked to DEWAT to treat the water, which could then be recycled for flushing. Communities contribute a small monthly amount to pay for annual maintenance of common septic tanks but also profit by way of sale of composted sludge, money that is reinvested in the community.

The success of these toilets has begun to catalyze housing upgrades. For temporary shacks, a core house design using columns is enabling the poorest to have a toilet and build a stable structure around it incrementally from small savings or housing finance. Local government in Agra has seen this as an opportunity to improve the city's overall sanitation and has developed an inclusive city development strategy to help build and retrofit 4,000 slum toilets, intercepting their direct sewage discharge into drains, and transporting it through appropriate channels. Ultimately, this will revive Agra's sewage-choked storm water drainage system.

*Source:* Dr. Renu Khosla, Director, Centre for Urban and Regional Excellence (CURE).

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## Policy challenges and implications

The MDGs are about meeting the basic needs of all citizens in developing countries. The two facets of urbanization that matter the most for both poverty reduction and attainment of the MDGs are: (i) managing the factors that affect urban population growth and expand the boundaries of urban areas; and (ii) understanding the spatial location of poverty. As these facets differ significantly between countries, country specificity should not be ignored in the design of any country policies aimed at attaining the MDGs.

The key relevant factors identified in this report that can inform policy makers and others addressing these challenging facets include the following:

- The natural increase in the urban population accounts for at least 50 percent of urban population growth in all countries, on average. Urban population growth is also affected by the reclassification of rural boundaries. Migration is a third factor in urban population growth. The weight of each these factors in affecting urbanization depends on country circumstances.
- Rural-urban migration can, *ceteris paribus*, lead to a reduction in rural poverty but migration is not uniform across regions or countries. It is highest in LAC and EAP and lowest in South Asia; SSA falls somewhere in between LAC and South Asia. Governments play an important role in urban poverty reduction when they facilitate migration. Whether rural-urban migration increases or reduces urban poverty depends upon whether migrants contribute to the positive or negative aspects of urbanization.
- Poverty is not spatially bi-polar, but distributed along a spectrum. Rural areas are the poorest and lie at one end of the spectrum; megacities and large cities are the richest and form the other end, and smaller towns of varied sizes and slums in larger cities lie in between. The implications of the spatial location of poverty along a spectrum are non-trivial. The challenge for the MDGs is to design poverty reducing and service delivery strategies that take a comprehensive approach towards the spectrum along which poverty is located.
- In a large number of countries, the majority of the urban population resides in the larger cities, as for example in India and Vietnam, but the majority of the urban poor lives in smaller towns that are often as poor as rural areas. Ignoring the growth of urban poverty in smaller towns can undermine efforts to reduce overall urban poverty as well as overall poverty.
- The spatial distribution of poverty in SSA is distinct from that of other regions. SSA's poor are disproportionately concentrated in rural areas. Of the small proportion located in urban areas, the majority are located in the largest city, usually the capital. Population density in SSA is sparse, which makes it difficult and costly to deliver network-based services that benefit from scale economies.
- Rural poverty is distinct from urban poverty but there is a strong interdependence between rural and urban economies. As 75 percent of the poor worldwide still reside in rural areas, the role of rural poverty-reducing policies must be central to any policy approaches aimed at attaining the MDGs.
- The necessary ingredients for strong and sustainable linkages between rural areas and smaller towns are a rich rural hinterland that can feed urban areas and access to urban markets where rural households can trade. Rural growth also has a positive impact on urban poverty reduction.

Policies that spur this process include: an increase in rural productivity through the introduction of new farm technologies and investment in the human capital development of rural residents; removal of land market distortions; improved connectivity with urban markets; and a fostering of non-farm activity and rural-urban migration.

- Rural-urban migration is an equalizer with the potential to bridge rural-urban disparities in incomes and access to basic services, alleviating rural poverty as illustrated in Tanzania. Removing policy-induced constraints to rural-urban migration can enable urban growth to reduce rural poverty. Policies that remove land market distortions and facilitate access to markets can foster migration.
- At least seven of the MDGs are related directly to the delivery of basic services, and the poverty-city size gradient is a strong marker of access to services. Invariably, rural areas are the worst off and smaller towns and slums have poorer access to basic amenities than large cities. Problems in service delivery are related to both quantity and quality, and the poverty-city size gradient applies equally to access to infrastructure services such as provision of safe water and sanitation.

The implications of urbanization for the provision of MDG-related services to all individuals in developing countries are complex and need to be considered in a framework that appropriately recognizes the factors described above. Governments have two main policy levers with which to achieve the MDGs: (i) the suite of macro policy instruments that spur agglomeration economies and job creation; and (ii) public investment in MDG-related services.

The first-best solution is to facilitate access to *all* MDG-related services for *all* poor through expert management of the urbanization process. This implies either: (i) accelerating investments in the factors that fuel the urbanization process (the subject of Chapter 3) and attract the poor to cities; or (ii) equalizing service delivery wherever the poor are located (i.e., in rural areas and small towns as well as slums).

Not surprisingly, the first-best solution is unviable for several reasons: (i) resource and capacity constraints; (ii) not all of the rural poor can migrate to cities at once and even if they could, congestion effects would likely worsen urban poverty and undermine the urbanization process; (iii) even if ideal cities were created, not all of the rural poor would be willing to forgo their rural assets and migrate; and (iv) even if the poor wanted to migrate to larger cities, it is unrealistic to presume that they would find productive jobs if they did not arrive endowed with at least some basic human capital.

The second-best approach is to prioritize between the type of services, delivery location, and timing. Three types of policies could be leveraged:

- In areas where migration is significant and poverty is more bi-polar, boosting the urbanization process in large cities through better delivery of MDG-related services and provision of incentives for job creation would make large cities more attractive and would motivate the rural-urban migration. Migrants would enjoy the benefits of urban living and would presumably step out of poverty and towards greater prosperity. For this to happen, poor migrants need to have a basic stock of human capital (i.e., be healthy and have a basic education). Thus public investment in primary education and health care should be directed to the poor both in small towns and in rural areas.

- In countries where: (i) migration is limited and reclassification and natural population growth dominate the expansion of urban boundaries; (ii) population density is high; and (iii) the poverty-city size gradient is dominant, the poverty differentials between poorly served areas and larger cities are unlikely to shrink sufficiently to foster the attainment of the MDGs. In these situations, policies that facilitate migration will help. Progress towards the MDGs would be accelerated by delivering services wherever the poor are concentrated, otherwise both rural and urban poverty will remain grounded wherever it is.
- In situations where people are stuck in rural towns, with little prospect of moving on, policies should focus on improving connectivity with other urban centers. Poverty in rural towns is often high, and the quantity and quality of services there differ little from those in rural areas and lag behind those in more mature urban settlements. In these cases, measures to better connect the activities in rural towns with the economies of larger cities become paramount.

In all three cases, investment in portable services (education and health care) would optimally be provided wherever the poor are. But in countries with high migration and low population density in rural areas, delivery of non-portable infrastructure services in larger cities would be more cost-effective and more supportive of urbanization and industrialization and could be prioritized as such. Countries in SSA would typically fall in this group.

Finally, a reduction in the number of slum dwellers is a dedicated MDG and needs a dedicated approach. To address the unique challenges associated with slums, policy solutions must:

- Focus on improved management (discussed in Chapter 3) and resist the temptation to simply arrest migration.
- Tie policies for slums to those of the city as a whole with respect to land tenure, particularly in terms of land pricing, connectivity of residential and commercial urban space, and above all, the appropriate balance between economic and population density. A “silo” approach will lead to a lose-lose solution for cities and slums.
- Take advantage of slums’ proximity to the city so that the unit costs of extending access to basic health and education services to slum dwellers are relatively low.
- Expand the supply of public toilets and water to slum dwellers in creative ways (e.g., water fountains in public places) in the short term, recognizing that the permanent solution to water and sanitation is tied to the land issue.
- Make use of the fact that in most cases, slum dwellers are willing to pay a small fee to access basic services.
- Take a comprehensive approach to job creation that will support agglomerations economies, as the factors that fuel creation of better jobs for the city will also lead to jobs for slum dwellers.

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## Annex 2.1: Equalization of Health Service Delivery and Their Expected Impacts on the MDGs: A Simulation Exercise

Closing the rural-urban MDG and service gaps may represent a major challenge for many countries, especially if these gaps are large and the unit costs of services for rural populations are higher than for their urban compatriots. In the simulation exercise presented in this section, the broader economic consequences of closing health gaps in low-income countries are explored by adapting MAMS, a CGE model for country strategy analysis, to address rural-urban aspects of MDGs. The database used was designed to capture characteristics typical of low-income countries, including their MDG outcomes, sectoral shares in value-added, the degree of urbanization, and population growth.

The base simulation assumes: (i) an annual growth rate of 5.6 percent, following the trend of low-income countries since 2000; and (ii) “business as usual” in terms of government policies and spending, including borrowing that is consistent with debt sustainability. In the non-base simulations, for the period 2014-2030, it is assumed that the government gradually scales up its health services, either: (i) closing the gap between the level of per capita health services reaching rural versus urban residents; or (ii) closing the rural-urban gap in the under-five mortality rate (the U5MR), the outcome indicator of interest here. These efforts are undertaken using alternative sources for required additional financing (foreign grant aid, domestic borrowing, taxes, and reduced spending on infrastructure).

Under the base scenario, the major macro indicators (GDP, government and private consumption, and investment) all grow at annual rates of around 5 percent; in per capita terms, household consumption grows at an annual rate of around 3.1 percent, with a slightly more rapid rate for rural households (3.2 versus 3.0 percent). As shown in Figure A2.1, significant progress is realized for both poverty and the U5MR, while the rural-urban gaps narrow but still remain substantial.

In the first simulation (denoted *mdg4u+fg*), the government gradually raises per capita rural health services to the urban level while maintaining a growth rate for urban services that is sufficient to maintain the same reduction in the urban U5MR as under the base; i.e., the improvement in the rural population does not come at the expense of the health outcome of the urban population; additional foreign grant aid provides needed financing. As shown in Figure A2.2, this reduces the 2030 rural U5MR by slightly more than 5 points, closing roughly half of the rural-urban gap. Both rural and urban poverty rates are virtually unchanged. At the macro level, growth in government consumption increases by 0.6 percentage points (Figure A2.3), accompanied by a similar increase for government investment, with the increases directed to the health sector and financed by foreign grant aid, in 2030 raising the latter by 1.2 percent of GDP, to 5.1 percent (Figure A2.4). If the financing gap instead would have been met by concessional foreign borrowing, then the foreign debt of the government would have reached 43 percent of GDP in 2030 compared to 32 percent for the base scenario.

Instead of relying on foreign resources, the government may create the fiscal space needed for this increase in health spending by turning to domestic resources, including borrowing, or higher taxes (scenarios denoted as *mdg4u+db*, and *mdg4u+tx*, respectively). While the outcomes are very similar or the same in terms of the rural and urban U5MRs, these scenarios lead to higher urban and rural poverty

rates (Figure A2.2), accompanied by slower growth in private consumption; for the borrowing scenario, the poverty reduction and consumption outcomes are more negative while GDP and absorption growth rates also decline, as the private sector is deprived of investment funding (Figure A2.3). For both scenarios, the macro slowdown reflects the opportunity costs of reallocating resources to government health spending: less funding for domestic private investment and capital accumulation ( $mdg4u+db$ ), or reduced real disposable income for households, leading to losses spread over private consumption, investment, and capital stock growth ( $mdg4u+tx$ ).<sup>40</sup>

Under the preceding scenarios, the rural U5MR remains above the urban level, pointing to the fact that lacking government health services is only one of the factors behind the gaps between rural and urban health outcomes. However, more ambitiously, the government may decide to gradually raise government health services in rural areas to such an extent that by 2030 the U5MR of the rural population will have declined to the urban U5MR level in 2030 simulated under the base scenario; i.e., the government would try to make up for the other gaps suffered by the rural population by providing them with additional targeted health services while, at the same time, maintaining the same per capita real health spending for the urban population as under the base scenario. On the margin, the increase in real services per capita (or per avoided death) is higher under this scenario, reflecting the need to reach more disadvantaged population groups and to turn to more costly interventions, in effect reversing the initial discrimination against the rural population in health service provision. If foreign grants provide the marginal financing ( $mdg4r+fg$ ), then in 2030, these will have to increase by 5.6 percent of GDP compared to the base, to 9.7 percent of GDP. Compared to the base outcome in 2030, the intended reduction in the rural U5MR is realized, together with small reductions in the urban U5MR and poverty in both rural and urban areas (Figure A2.2). A strong growth increase is recorded for government consumption, along with more modest increases for private consumption, GDP, and absorption, the latter enlarged by the increase in grant aid (Figure A2.3).

It is difficult to reallocate this amount of resources to government health spending without negative repercussions. If the government relies on higher taxes ( $mdg4r+tx$ ), the increases in which in 2030 reach 7.6 percent of GDP compared to the base, these repercussions are felt in the form of a slightly higher urban U5MR and higher poverty rates, especially in rural areas (Figure A2.2), as well as in slower growth for private consumption (Figure A2.3). The reason behind a relatively strong rural poverty increase (for this and some of the preceding scenarios) is that government services, which were scaled up, are relatively intensive in the use of the more educated labor supplied by urban households, whereas private spending, which was scaled down, disproportionately reduces the demand for land and less educated labor, factors that provide a relatively large share of the incomes of the rural population.<sup>41</sup>

From a different angle, given inefficiencies in the government health sector in many low-income countries, it is possible to reduce the need for extra financing by raising efficiency. For a set of scenarios that raise the rural U5MR to the urban level by 2030, Figure A2.5 maps out combinations of: (i) average per capita foreign grant increases (in 2009 US\$) 2014-2030; and (ii) additional annual growth in

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<sup>40</sup> As a result of more rapid private consumption growth for  $mdg4u+fg$  than for the other scenarios, the health objectives can be achieved with a slightly smaller acceleration in government health spending and government consumption growth for  $mdg4u+fg$ .

<sup>41</sup> Additional simulations showed that the domestic resources that could be mobilized via increased government borrowing were insufficient to finance the health policy of the last two scenarios ( $mdg4r+fg$  and  $mdg4r+tx$ ).

government health service efficiency (covering efficiency of new investments, as well as of labor and capital use but excluding material inputs such as medicines). In the absence of a gain in efficiency, the grant increase in an average year is around US\$26 per capita (at 2009 prices; from the scenario  $mdg4r+fg$ ). The need for additional grant aid would be eliminated if efficiency grew by an additional 6.2 percent per year. While such rapid gains may be infeasible, additional growth of at least 1-2 percent per year may be within the realm of possibility.<sup>42</sup> Interestingly, the gains in reduced aid per additional percentage point of efficiency growth are diminishing – this is due to real exchange rate effects: at high levels, grant aid leads to strong marginal appreciation, with strongly reduced domestic purchasing power as the result.

In sum, these simulations explore the consequences of providing and financing government health services to reduce the U5MR of the rural population. The results suggest that if the government, by mobilizing required resources and/or raising its own efficiency in the health sector, manages to raise the level of real health services reaching the rural population, then it is possible to considerably reduce the rural U5MR. If the bulk of resources come in the form of foreign grants or efficiency gains, then progress in the form of a lower U5MR can come with broader repercussions that have a positive impact on other development indicators, including poverty reduction. However, if most additional resources have to be mobilized from domestic sources, then this progress would threaten to come at the expense of less progress in terms of poverty reduction and other indicators, illustrating the difficult tradeoffs faced by low-income countries and their governments.

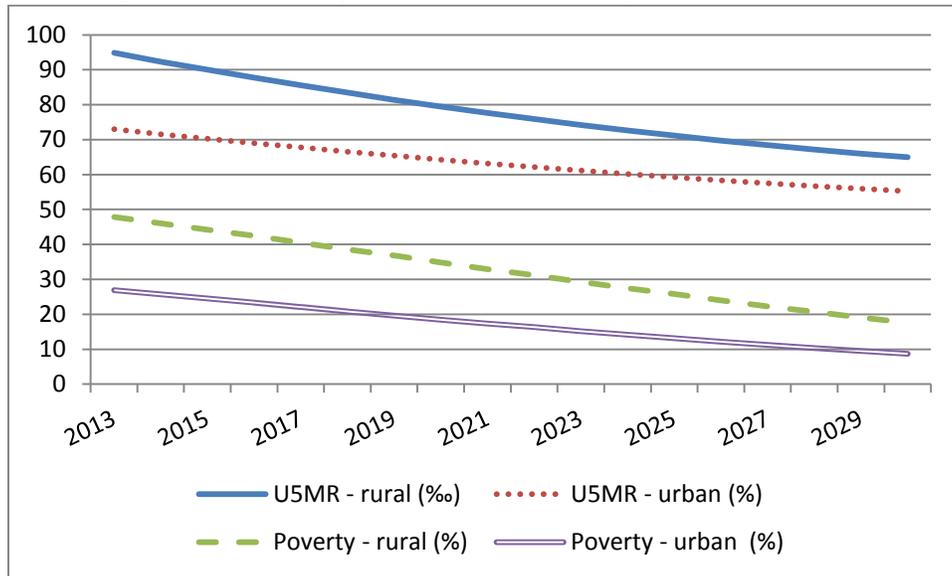
## Reference

Chaudhury, Nazmul, Jeffrey Hammer, Michael Kremer, Karthik Muralidharan, and F. Halsey Rogers. 2006. “Missing in Action: Teacher and Health Worker Absence in Developing Countries.” *Journal of Economic Perspectives* Vol. 20(1): 91-116.

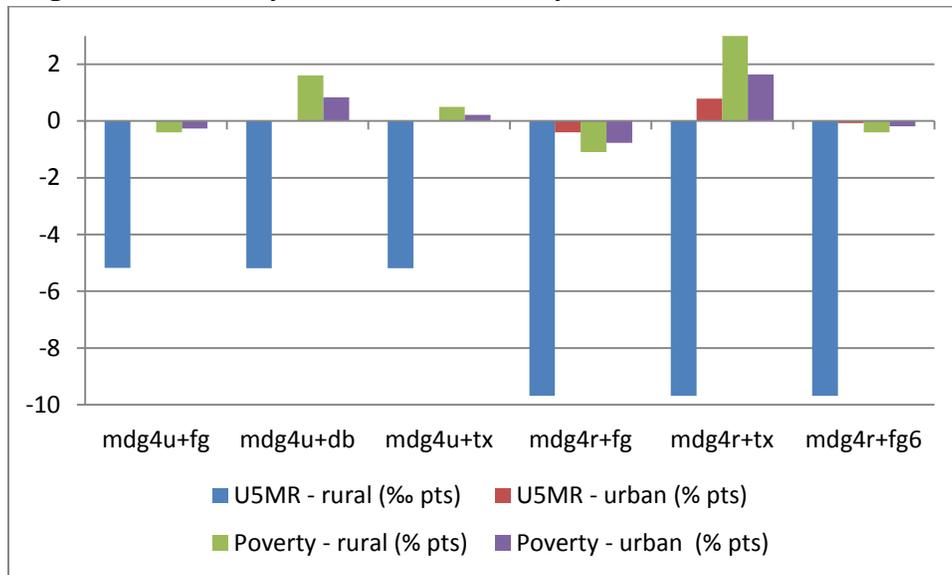
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<sup>42</sup> For example, on the basis of surveys in six low- and middle-income countries, Chaudhury *et al.* (2006) find that, on average, primary health workers were absent 35 percent of the time. Other things being equal, a moderate gradual reduction in their absenteeism to 17.5 percent of their time by 2030 would correspond to an annual increase in their productivity by around 1.5 percent per year.

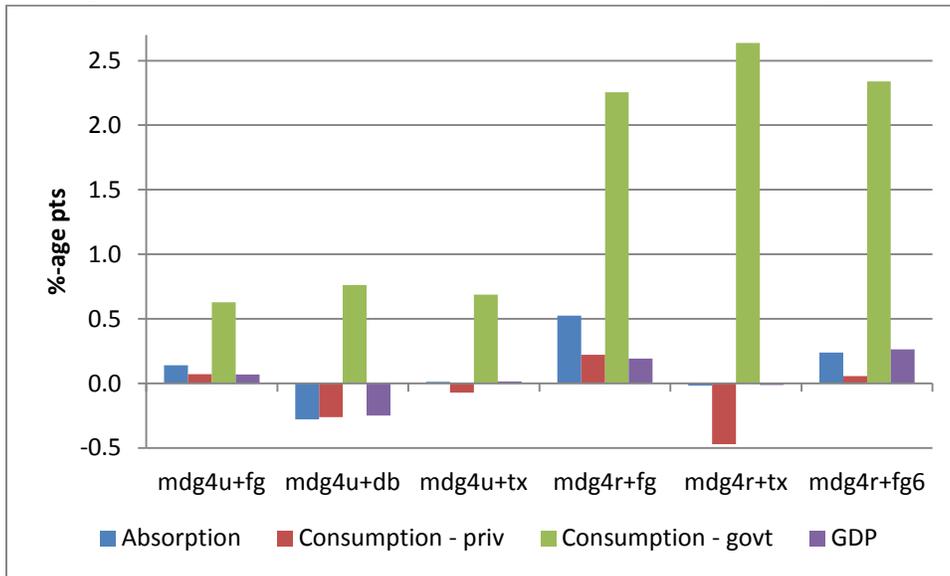
**Figure A2.1: Poverty and under-5 mortality for base simulation**



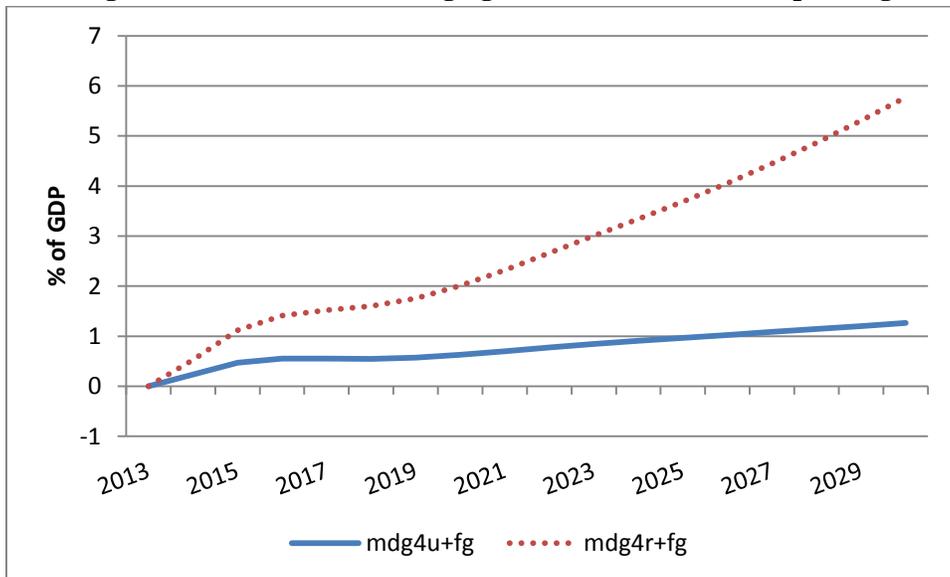
**Figure A2.2: Poverty and under-5 mortality – deviations from base in 2030**



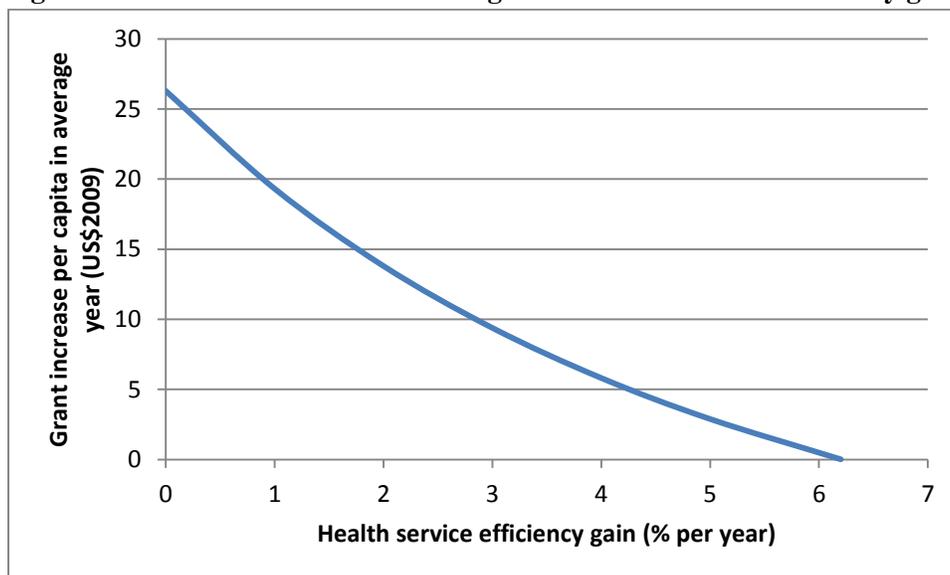
**Figure A2.3: Macro indicators – deviations from base annual growth**



**Figure A2.4: Additional foreign grants to finance health spending**



**Figure A2.5. Trade-offs between more grant aid and domestic efficiency gains**



### 3. How Can Urbanization Accelerate Progress Towards the MDGs?

#### Summary and messages

Urbanization matters. In the past two decades, developing countries have urbanized rapidly, with the number of people living in urban settlements rising from about 1.5 billion in 1990 to 3.6 billion (more than half of the world's population) in 2011. This has resulted in the fact that 2.7 billion people in the developing world are living now in cities. Citizens in urban areas are at an advantage compared to their rural brethren as not only are urban poverty rates significantly lower than rural poverty rates but also urban populations have far better access to the basic public services defined by the MDGs, such as access to safe water and sanitation facilities (Chapter 2).

Urbanization is rapidly taking place in the developing world. Of the anticipated population increase of 1.4 billion people between 2011 and 2030 in the developing world, 96 percent of them will live in urban areas. Henceforth, if the forces of urbanization are not managed speedily and efficiently, slum growth can overwhelm city growth, exacerbate urban poverty, and derail MDG achievements and reduce if not evaporate cities' comparative advantage regarding attainment of the MDGs.

Urban growth is not going to be limited to the megacities of the world though; rather, secondary cities such as Huambo in Angola, Fushun in China, and Surat in India— cities that few would be able pinpoint on a map — are going to growth at rapid speeds. The good news is that many of these emerging urban centers are still taking shape, providing policy makers with a unique but rapidly closing window of opportunity to get their cities “right” to enhance economic, social, and environment outcomes.

In many respects, the move to cities is entirely rational. Cities are the hubs of prosperity – over 80 percent of global economic activity is concentrated in cities (McKinsey Global Institute 2011).

The densities that cities offer can create scale economies that enhance job opportunities and productivity, as well as make it cheaper to expand services. Cities, through their density, make public services more accessible. For example, it costs US\$0.70 to US\$0.80 per m<sup>3</sup> to provide piped water in urban areas, versus US\$2 in sparsely populated areas (Kariuki and Schwartz 2005). Schooling and health care can be delivered at scale in dense environments, close to where people actually live.

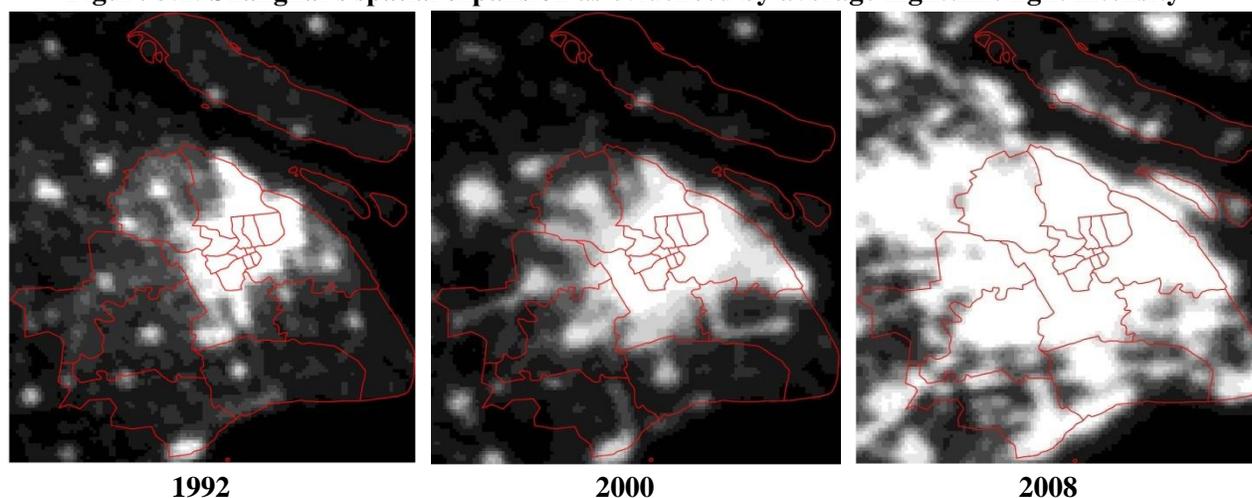
Urban densities can pull up rural areas. In fact, research in India has shown a growing link between urban development and a reduction of rural poverty following India's economic liberalization in the early 1990s – linked to higher demand for rural products and the provision of options for rural non-farm diversification (World Bank 2013a).

However, unregulated markets are unlikely to get densities “right,” as the economic productivity- and opportunity-generating aspect of increased density is an externality, whereas the increased costs of construction necessary for higher density are fully internalized by firms and households (Collier and Venables 2013). Supporting greater densities requires higher quality construction material and more

sophisticated buildings. In addition, complementary physical infrastructure is critical: roads, drainage, street lighting, electricity, water, and sewerage, together with policing, waste disposal, and health care. More rather than less public policy is needed to ensure that the productivity gains and services that cities can deliver are not overwhelmed by crime, disease, and squalor.

While a fully market-driven process could possibly gradually increase densities via land values over time, the long-lived and lumpy nature of urban investment inhibits such a process. A city's physical structures, once established, may remain in place for more than 150 years (Hallegatte 2009). The alarming news is that the doubling of the urban population in the developing world will be accompanied by a tripling in the built-up area of cities, from 200,000 to 600,000 square kilometers. As an example, consider Shanghai, which has rapidly expanded over the past 20 years (Figure 3.1). Such rapid population growth accompanied by an even faster spatial expansion of cities is likely to lead to low density development dominated by individual-vehicle transportation – a largely irreversible pattern (World Bank 2012a). This will run the risk of dampening density-induced productivity and service delivery efficiencies. An additional consequence of rapid urban growth is worsening air quality; a recent study of the 189 largest cities using satellite data found that air quality worsened between 2002 and 2010, particularly in the largest cities of the Indian subcontinent, parts of Africa, the Middle East, and North China – places experiencing rapid urban growth (Alpert *et al.* 2012).

**Figure 3.1: Shanghai's spatial expansion as evidenced by average nighttime light intensity**



Source: China Data Center at University of Michigan.

Emissions from fossil fuel burning include fine particulate matter (PM10 and PM2.5), carbon monoxide, nitric oxides, and sulfur dioxide, which can cause allergies, respiratory problems, cardiovascular disease, and cognitive deficits. The impacts are significant. In Russia, a conservative estimate suggests that annual health damages from fossil fuel burning amount to US\$6 billion (Markandya and Golub 2012). The social cost of transport in Beijing is equivalent to about 7.5 to 15 percent of its GDP, with about half of that stemming from air pollution (Creutzig and He 2009). The largest share of these costs comes from increased mortality. Globally, acute respiratory infections associated with air pollution cause about 20 percent of all under-5 mortality (Mehta *et al.* 2011). In the FYRO Macedonia, a country of about 2 million people, an estimated 1,300 premature deaths are caused by air pollution. Dhaka, Beijing, Karachi, Cairo, and Delhi see an estimated 3,500 to 7,000 premature deaths annually from cardiovascular disease

due to air pollution (Gurjar *et al.* 2010). Karachi has the highest overall mortality, at 15,000 per year. This is close to the excess mortality of 13,000 deaths caused by the “Great Smog” in London in 1952, evidence that many cities in today’s industrialized countries have gone through similar stages of excessive pollution. Managing environmental quality alongside enhancing urban productivity is critical.

Cities can accelerate economic and social progress when complementary improvements are made along two fronts:

- *Job creation, investment, and growth*, which depend on the density of cities and their linkages with the rural economy. Enhancing job opportunities in cities necessitates careful thought about coordinating land management, housing, transport, communications, and infrastructure improvements (World Bank 2013a). Urbanization generates an increase in the demand for land, and a clear definition of property rights along with robust systems for assessing land values are key for land redevelopment. For example, Korea encouraged the development of a cadre of property appraisers during the 1970s. This has to be combined with the development of reliable and affordable public transit to physically connect people with jobs as it increases the effective distance that a worker can travel to access job opportunities. Complementary improvements in communication and interregional transport can make it easier for neighboring rural areas to be integrated with the urban economy.
- *Expansion of basic services, such as those reflected by the MDGs, across cities and rural areas*, so that when people move to cities, they are pulled by the opportunities that cities can offer, not pushed from the countryside in search of basic services they have been denied. Improvements in basic services such as water, sanitation, education, and health are essential for improving living standards and workers' health and education, as was done in Colombia, which systematically improved and converged basic service levels across the country. In 1964, only half the residents of Bogotá and other large cities had access to water, electricity, and sanitation; today there is nearly universal access in cities of all sizes, a convergence that took more than 40 years (Samad *et al.* 2012).

However, many developing countries have been unable to provide a coordinated package of physical infrastructure and social services (see Box 3.1). In part, this is because many of these are network goods that cannot be provided by each household or community individually. Even where they can be supplied by each individual household or a community, as with sanitation, there are substantial externalities. While each infrastructure sector and service can be addressed by appropriate government policies, addressing only one or two of them has little payoff if the others remain unresolved (Collier and Venables 2013). And because different infrastructure and derived services generate varying degrees of externalities, the issues faced by each sector differ considerably from one another, and are typically the responsibility of distinct branches of government with little natural collaboration. Getting the highest level of political support to enable cross-sectoral and intergovernmental coordination is critical for getting urbanization right.

### **Box 3.1: Bangalore Has Nurtured Skills – But Must Now Tackle Infrastructure**

An analysis of the factors that have contributed to Bangalore's success shows that in 1998, the city's incomes were 24 percent higher than the national average. In 2005, they were nearly 70 percent higher.

The skills of the city's residents are the bedrock of its economic success. These skills have early origins, with the Maharajas of the princely state of Mysore instituting compulsory education and building the University of Mysore and Bangalore's engineering college. This was the starting point for the cluster of educated engineers that persists to this day. Building on an initial corpus of engineering expertise, firms such as Infosys were attracted to Bangalore, jumpstarting a virtuous circle where smart companies and smart workers came to Bangalore to be close to one another.

However, Bangalore's economic success is creating infrastructure problems, including poor water quality, traffic congestion, and housing shortages. The water system is strained – 30 percent of city residents use polluted groundwater; the sewer system does not reach a large part of the city; and average commute times are more than 40 minutes because jobs are dispersed from the city core. If the water problems or commuting times get worse, skilled people – the city's main asset – will leave for cities that offer better amenities. How Bangalore improves the quality of life for its residents will have a considerable bearing on how bright Bangalore continues to shine.

*Source: Glaeser 2010.*

## **Framework for urbanization policy**

The policy framework used here draws heavily on the 2009 *World Development Report: Reshaping Economic Geography* (World Bank 2008) and subsequent country level diagnostics under the World Bank's Urbanization Review Program, whose lessons are synthesized in *Planning, Connecting, and Financing Cities – Now* (World Bank 2013b). The 2009 *World Development Report* (WDR) looked at urbanization trends and policies worldwide and proposed a three-part policy framework for urbanization. First, institutions should provide the foundations for liberalizing the movement of people and goods and easing the exchange and redevelopment of land – enabling vast economic gains. Second, investments respond to the needs of residents and businesses, especially for basic and connective infrastructure. Third, targeted interventions respond to the needs of the poor and people in marginal locations or address individual behaviors that endanger health, safety, or the environment. Applying the 2009 WDR policy framework, the World Bank's Urbanization Reviews offer policy makers diagnostic tools to identify policy distortions and analyze investment priorities.

Each review starts by assessing a country or region's spatial transformation: how the urban economy is evolving; how demand for the city is changing with economic development; the pace of new arrivals; and how these new arrivals into the city are finding places to live and commuting to their jobs. It then compares the city's observed patterns with benchmarks in other places or with past conditions. Such comparisons help reveal how policy distortions constrain urbanization and how investment shortfalls limit the benefits from it. Once the review has identified the possible constraints and shortfalls, it proposes policy options. It aims to show how a city can harness economic and social benefits not just today, but in the future as economies grow, technologies change, and institutions are strengthened. Urbanization Reviews have been piloted in over 12 countries at varying stages of urbanization, including Uganda and

Sri Lanka (where urbanization is nascent), China, India, Indonesia, and Vietnam (where it is rapid), and Brazil, Colombia, Korea, and Turkey (where it is mature).

At the heart of the diagnostic approach used in the Urbanization Reviews are three main dimensions of urban development (Figure 3.2):

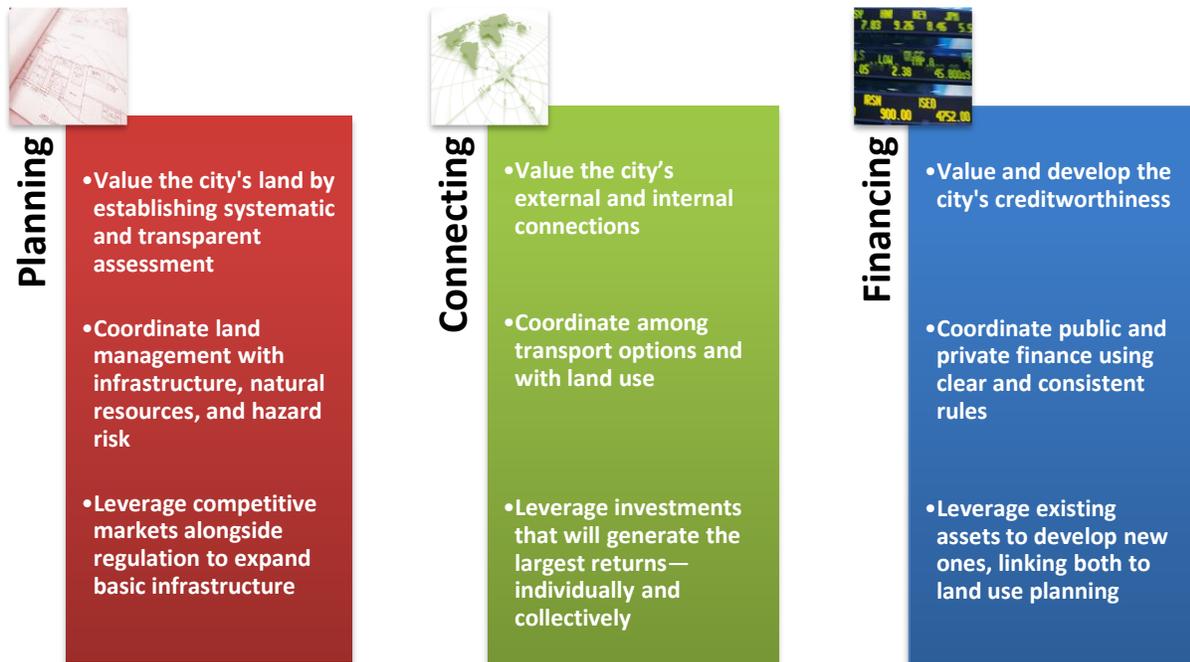
- *Planning* – charting a course for cities by setting the terms of urbanization, especially policies for using urban land and expanding basic infrastructure and public services.
- *Connecting* – making a city’s markets (labor, goods, and services) accessible to other cities and to other neighborhoods in the city, as well as to outside export markets.
- *Financing* – finding sources for large capital outlays needed to provide infrastructure and services as cities grow and urbanization picks up speed.

Planning, connecting, financing – these are terms that policy makers use on a daily basis. Of the three, a major finding from the Urbanization Reviews is that regardless of the level or speed of urbanization, planning for land use management must be the top priority. By clearly defining property rights, and putting in place effective systems for land use that are coordinated with infrastructure, transport, and natural resources, policy makers can help their cities attract private investment, connect people with jobs, and reduce environmental, social, and natural hazard risks. With much of urban growth in developing countries likely to take place in secondary cities, strengthening land management provides a unique, albeit rapidly closing, opportunity to shape urban design so that people do not have to spend a significant part of their day traveling to and from work.

Of course, financing rapid urban growth is challenging, as large upfront capital investments are needed to build systems for transport and water, solid waste management, and sewage removal and treatment. But financing can become more sustainable through taxes that come with increased economic growth, and also with the ability of mayors to leverage land markets and approach local currency debt markets. An important point is that financing should be closely integrated with a city’s plans for managing growth. Related, the process of urban management should involve as many private actors as deemed necessary to ensure that the city becomes (again) or remains competitive and consequently an engine of growth and well-being.

However, policy makers often place financing first without fully considering a city’s plans and connections. And the lack of such coordination will be regretted by later urban generations. For example, in Hanoi, Vietnam, a projected new mass transit system will extend in several directions from today’s central business district – but it will not reach an emerging second central business district southwest of the city, where dense housing developments called New Urban Zones are already being built (World Bank 2011).

**Figure 3.2: A framework for urbanization policy: planning, connecting, and financing**



*Note:* This framework draws on World Bank 2012b and the findings from various country pilots under the Urbanization Reviews.  
*Source:* Urbanization Review team.

Similarly, Colombia's urban development challenges arise from problems of policy and planning. One of Latin America's most decentralized countries, Colombia has more than 1,000 municipal governments with parallel responsibilities—basic infrastructure service delivery, land use and economic development, and social service provision. Urban areas comprise multiple municipalities: Bogotá, for example, contains seven. These municipalities lack mechanisms to coordinate policy and planning across their boundaries. As a result, Colombia's metropolitan areas are crippled by inertia—unable to coordinate their land use policies, or plan for strategic investments, at the metropolitan or regional scale that is demanded by a growing urban economy.

Uganda's 1995 Constitution created private land ownership and abolished land leases vested with local urban bodies. Local governments were fiscally starved, unable to acquire land or protect rights-of-way for infrastructure improvement. And land transactions generally were hampered by: poor tenure security (only 18 percent of land is registered and titled); the lack of a credible system for valuing land; low incentives for landowners to rent their land; and high entry costs for land development ventures. To remedy the situation, especially in the metropolis of Kampala, Uganda urgently needs a credible system for documenting and valuing land. To be sure, local urban bodies also need financing support—to buy land and pay for infrastructure. But no amount of financing alone will solve Uganda's problems (World Bank 2012c).

## Planning cities

Planning is fundamental to agglomeration economies in three ways. First, land use requires effective systems for land valuation. Second, land use must be allocated in a way that it allows for infrastructure improvements. Third, the most basic infrastructure services – water, energy, sanitation, and solid waste management – need to be provided for all residents, urban, peri-urban, and rural alike.

### Set up systematic and transparent systems for valuing land and enabling transactions

The use and reuse of land is central to a city's expansion and development. For economic efficiency, land should be able to shift among various uses – though public intervention may be required to offset market failures (Henderson and Wang 2007). Urban land markets should efficiently allocate land between urban and rural uses (with incentives to conserve farmland and green space) and within urban areas (to prevent disordered land use and underserved neighborhoods).

What is the key to efficient land use? The answer is the price of land. Institutions that improve the information foundations of the valuation process, including having a trained cadre of appraisers in property valuation, contribute to ensuring transparency in the valuation process and to making information about land values widely accessible. In Korea until the early 1970s, local government officials assessed the market value and replacement costs of assets for land acquisition purposes. In 1972, the government introduced the Basic Land Prices system to improve assessments. In this new system, land and buildings had to be assessed by certified private appraisers rather than government officials. Two such appraisers had to provide estimated values for the property and the final value was calculated as the average of the two values. If the two appraisals differed by more than 10 percent, a third appraiser was selected and the average recalculated. Since 2003, a third appraiser may be recommended by affected individuals as well (World Bank 2013a).

Developing countries often lack the systems to record and manage information on land transactions. The data may not, for instance, reflect the true price of land because of black market transactions to save on duties or heavy public subsidies on housing and land use. Land registries are often archaic and lack the dynamic functions that allow them to be searched or updated quickly. These deficiencies translate into a dearth of data on real estate prices, preventing analysis that is critical for appraising land values, with heavy implications for real estate-based local financing. Land valuation is integral to local revenue generation since land values form the basis for activities such as property tax collection and land sales or leases.

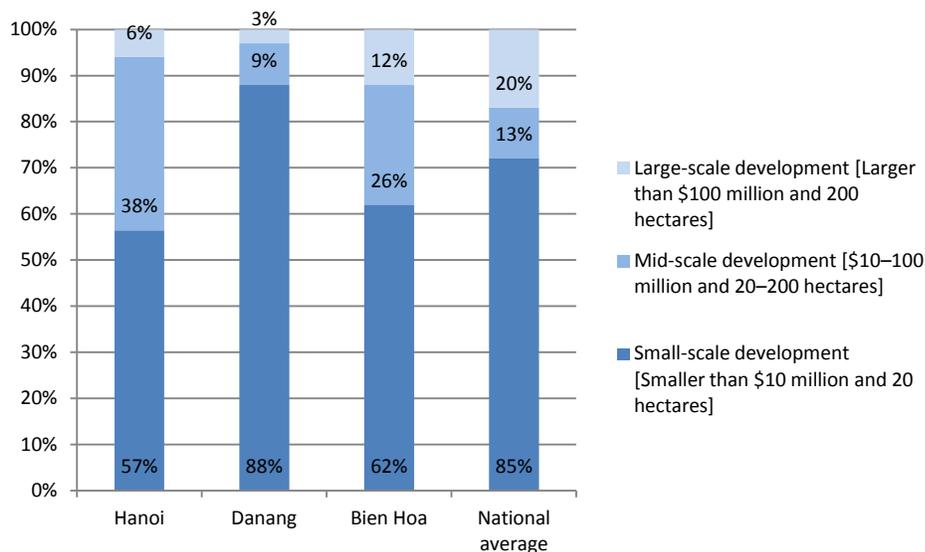
Take India, where such information systems are in their infancy and the government often acquires land for industrial and infrastructure development. Farmers and other landowners are compensated with payments benchmarked on the stamp duties – a land transaction tax. But since the marginal rate for stamp duties has been as high as 12 percent historically, land and property values have long been underreported (World Bank 2013a).<sup>43</sup> Now, as India's policy makers amend the rules for changes in land use, the lack of independent and reliable land valuations is likely to result in public discontent and conflicts over land.

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<sup>43</sup> In the U.S., transaction taxes are around 1–2 percent of property values.

In Vietnam, too, official land prices fail to reflect demand. The country has two kinds of prices for land transactions. First, there is the market price – the higher of the two. Then there is the imposed land price, a much lower value used by the government in acquiring land and allocating it to developers and investors (World Bank 2011). Such an inequitable system generates resentment over land acquisitions: over 1996–2005, there were more than 12,000 complaints. And conflicts over land, in turn, hinder the consolidation of plots for industrial development. More than 85 percent of available plots in Vietnam are smaller than 20 hectares – but industrial parks and districts typically need 150-200 hectares of contiguous land (Figure 3.3). So the country’s two-price system impedes efficiency and economic development.

**Figure 3.3: Vietnam’s dual land price system creates problems for the assembly of large plots of land needed for industry**



Source: World Bank 2011.

In countries where land valuation is successful, techniques are standardized to enable appraisers to arrive at uniform and transparent valuations. In the U.S., most states require that appraisers and assessors be certified. Appraisers generally work for private clients to determine the market value of property for real estate transactions, while assessors generally work for the government to determine property values for tax purposes (U.S. Department of Labor 2010). Both must follow the same regulations in valuing real estate. However, for practical purposes and to avoid overestimation of prices, property prices for tax purposes are often set at about two-thirds of actual market value. In Bogotá, property values are usually set at 70-80 percent of estimated market value.

Public land valuation in developing countries is fraught with challenges, including the cost of hiring private assessors (as these countries lack standardized public valuation methods), the need to update land price data, and the fact that intergovernmental transfers of public land are often recorded as a zero value transaction. These challenges can be overcome, however, as seen in at least two cases of innovation in public land valuation. Kuwait now requires two separate private appraisals for public-private partnerships (PPPs). And South Africa mandates that public land be taxed the same way as private land, which means that public land undergoes the same valuation processes (Peterson and Kaganova 2010). Yet many other developing countries still struggle to value public land, and auctions are often used to reveal land values.

In Germany, federal regulation governs private land valuation.<sup>44</sup> Germany has local land valuation boards that are charged with collecting and maintaining land price data as well as disseminating land price information (Lozano-Gracia *et al.* 2013). The U.S. allows each state to define its own method for private property valuation. In most cases, states delegate this power to local governments, leading to a vast array of approaches. While the most common is the market value (or sales comparison) approach, there are at least two others: the cost approach and the income approach. All three approaches are often used in parallel to estimate property values. The state of New York, for example, uses these methods for different property categories. It follows the sales comparison approach to value small residential properties and vacant land, using sales data of comparable properties for the previous three years. It adopts the income approach to value offices and businesses, taking an estimated income and dividing the net income by a capitalization rate. It uses the cost approach for new construction and renovations and for special properties such as stadiums, museums, and places of worship (LaFuente 2009).

Complementary policies that assign property rights and encourage trade of land are also needed to help settlements respond to the changing needs of the market. Fluid land markets help the transition out of agriculture, where rural land can be sold and/or rented for urban uses, and rural residents can seek more rewarding opportunities in non-farm activities in urban areas. For instance in Vietnam, strengthening of land tenure security quadrupled participation in rental markets from 3.8 percent in 1993 to 15.8 percent in 1998 and resulted in an increase in rural urban migration from 29 percent in 1993 to 64 percent in 1998. In addition, both rental and sales markets had positive impacts on productivity.

In conclusion, getting land markets and land management to work better requires improving and upgrading and/or reforming the underlying related legal system. Urbanization will increase the demand for land, and governments at the national and subnational levels will employ instruments such as land acquisition and land readjustment for accommodating urban expansion, or land exactions for financing infrastructure. Strong legal systems and credible institutions will be a pre-condition for success. In particular, these include carefully designed laws to assign and protect property rights; institutions that enable independent valuation and public dissemination of land values across uses; and a strong legal framework supported by a healthy judicial system to handle disputes and oversee the process.

For land acquisition, courts need to provide guidance in terms of the legal scope of eminent domain. Given that the definition of public purpose constantly evolves, having a rigid and exclusive list of public purposes will pose stringent barriers to urban expansion. As an alternative, a flexible definition of public purpose can be combined with a strong judicial system to guide and evaluate acquisition decisions on a case by case basis. If a flexible definition is used, it becomes increasingly important to provide a clear definition of the process to adjudicate conflicts in cases where the "public purpose" of a particular acquisition is questioned, as well as to establish the institutions that guarantee that affected parties can voice their concerns.

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<sup>44</sup>“Verordnung über Grundsätze für die Ermittlung der Verkehrswerte von Grundstücken,” Werttax, [www.werttax.de/downloads/wertv.pdf](http://www.werttax.de/downloads/wertv.pdf).

## Coordinate land management with infrastructure, housing, and transport

### *Manage densities*

Just as valuing land and assigning property rights are challenges for accommodating urban expansion, so are managing densities within cities and finding ways to finance urban expansion and city renewal. One widely used tool for managing densities is the floor space index (FSI).<sup>45</sup> This is the ratio of the gross floor area of a building on a lot divided by the area of that lot. So, for example, if the FSI in an area of a city is 1:1, developers can only put up a building with a gross floor area less than or equal to the total lot area. While in some cases it may be possible to build a one-story building that covers the lot entirely, thus achieving an FSI of 1:1, developers typically construct buildings with a “footprint” or “plinth” that covers less than the whole lot and build structures with more than one story. For example, a developer could cover 25 percent of the lot and build a four-story building and still meet the FSI of 1:1.

Other planning regulations include setbacks (minimum distances to the front, rear, and sides of a plot) and maximum building heights. Both are designed to protect adjacent properties and preserve access to sun, air, and open space (parks and plazas). Finally, plot coverage ratio regulations limit the total area of a plot that can be developed (World Bank 2013b). It is very important to highlight that there is no such thing as an optimal FSI. The “right” FSI for a specific area will depend on the existing spatial structure of the city, the street patterns and widths, the level of infrastructure (is there enough capacity to accommodate higher density – higher FSIs?), and cultural and social factors (are skyscrapers acceptable?) (Bertaud 2004).

Although these regulations exist for good reasons, they often have unintended consequences. If an area’s FSI is set far below the level at which investors might otherwise develop it, this repression of supply can push people out to other areas – and the increased demand for those other areas can raise prices across the city (Annez and Linn 2010). Similarly, if the FSI is a uniform limit, it may increase housing prices by limiting the supply of land that would otherwise be built up. It may also encourage the allocation of land and buildings to less productive uses. Beyond slowing city growth in these ways, a uniform limit can also push poor households to distant suburbs, adding to their poverty by increasing their commuting costs and times. When households have no choice but to locate themselves near jobs, they often join hazard-prone informal settlements.

Consider South Africa, where the government has focused on provision of subsidized housing, first introduced as part of the Reconstruction and Development Program (RDP). However, the benefits from the RDP to living standards have been questioned. The most common complaint heard is that households who receive RDP housing are not satisfied with their dwellings as these are often far from employment centers: the new houses were often built in the “old” apartheid locations (which were deliberately sited far from urban centers and white neighborhoods). In addition, households most often do not receive title deeds immediately, but are merely administratively allocated these houses, with the condition that they cannot be sold or rented for a period of eight years, recently changed to five years. And even if they do receive title, this condition is attached to the title. Furthermore, even after the five year period, the government has a pre-emptive right (the right of first refusal) on the sale of the property. In other words, poor location and lack of fully tradable property rights are often cited as reasons for the limited impact of RDP housing.

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<sup>45</sup> Also known as the floor area ratio.

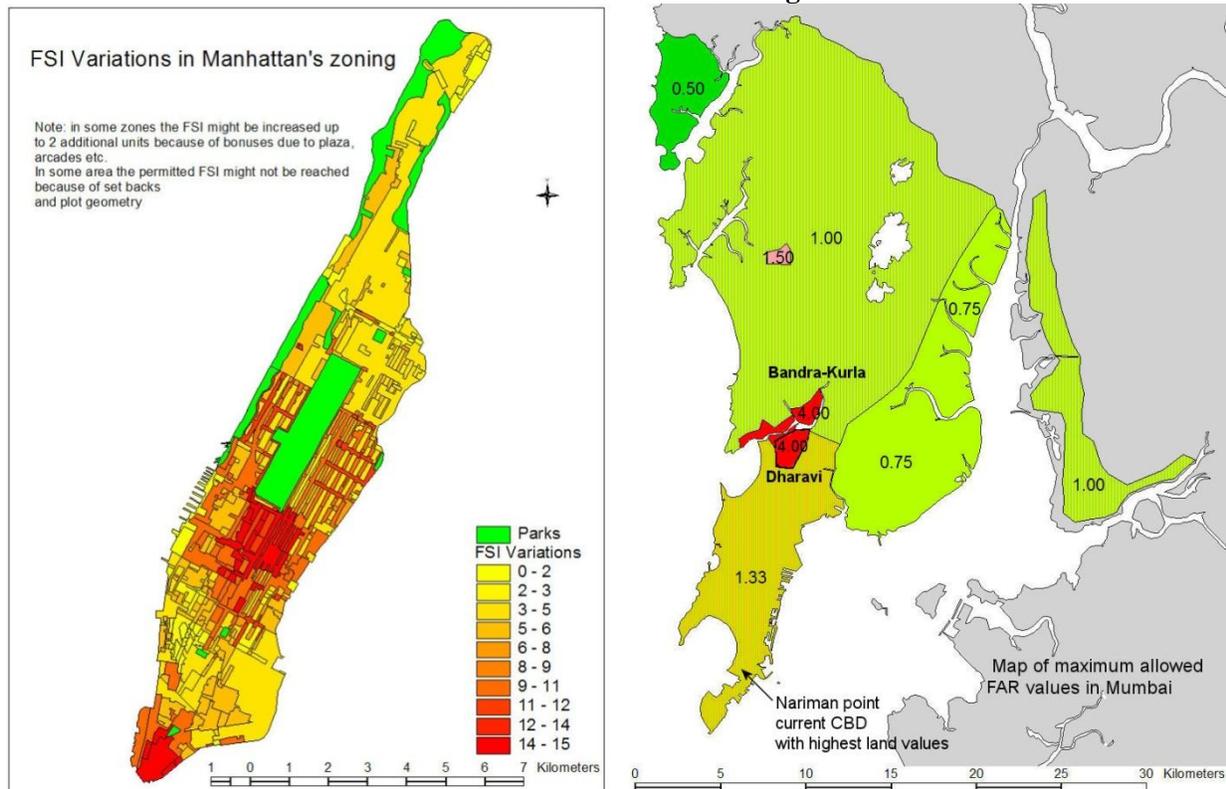
### *Integrate land management with infrastructure*

A central problem of urban planning is that of matching land use and infrastructure for the best possible outcome. Higher densities generate a greater need for infrastructure services (electricity, water, sewerage). But they also support environmental sustainability in being better suited to public transport. To be sure, density must not overwhelm infrastructure. Yet it is equally important not to underuse infrastructure, imposing low density caps where infrastructure can support higher ones.

To see what is at stake, compare Manhattan – New York City’s archetypal borough – with Mumbai (Figure 3.4). Manhattan’s density zones are typically small. Its restrictions on land use vary with street width and capacity, with infrastructure capacity, and with historical land use patterns (commercial office districts typically have higher FSIs than residential districts). This granularity helps to make Manhattan a good example of integration between land use and infrastructure.

In contrast, Mumbai’s density zones are large – uniform across much of the city – and densities are generally low. India’s urban planners justify such low formal densities as necessary to avoid overburdening existing infrastructure, which is severely limited. Rather than increase formal or planned densities, they have tried to preserve urban areas by pushing development out to new towns and suburban industrial estates – disconnecting people from job opportunities (World Bank 2013a). But this strategy ignores an opportunity: India’s cities could instead use rising land values to finance better, higher capacity infrastructure, to increase office space, and to add affordable housing for low- and moderate-income groups.

**Figure 3.4: New York's density management is granular and integrated with infrastructure while Mumbai's is coarse and not integrated**



*Note:* In some zones, the FSI might be increased up to two additional units because of bonuses due to plazas, arcades, and the like. In some areas, the permitted FSI might not be reached because of setbacks and plot geometry.

*Sources:* New York City Planning Department 2011 (left); Bertaud 2004 (right).

Keeping densities low and uncoordinated with infrastructure suppresses economic growth, most importantly exacerbating housing shortages and affordability. Cities' plans and zoning designations need to reflect market realities. If a city does not zone enough land for a particular use, the supply of land for that use will be constrained, causing land prices to rise. It is thus important that the master plan (including zoning designations) be based on market demand and that land use and densities reflect market realities. The consequence of master plans that artificially limit land supply can be soaring land prices. When plans underestimate required land uses, such as residential, industrial, commercial, and services, land prices for parcels zoned as such tend to sell at higher prices than would be set in the marketplace. In many cities in the developing world, urban planning consists of designing the expansion of cities using norms and spatial choices that reflect the preferences of urban planners rather than consumers' demand responding to supply constraints. This results in master plans becoming ineffective for both forecasting and guiding urban development (Box 3.2).

### **Box 3.2: Do Cities Need Master Plans?**

Instead of a large effort conducted every ten years, it may be better to produce a much simpler spatial strategy document that could be updated every year by staff of a city's urban planning department. The emphasis of such a document would be on the current spatial situation and spatial trends. Its main objectives would be on ensuring housing and land affordability and adequate mobility. Such a process would focus on analyzing real estate prices and supply and demand constraints for all income groups, firms, and households. The plan would cover three topics: (i) land use and spatially distributed demographics; (ii) road and transport networks; and (iii) land use and development regulations. Rather than attempting to cover all sectors, when the spatial strategy is approved by government, it could be distributed to line agencies that have the technical expertise to develop plans consistent with their program budget constraints, investments that are consistent with the spatial distribution of the population. It is important to provide the line agencies with a constantly updated spatial distribution of populations so that they can adjust to their investment programs to meet current and future demand.

This is not a revolutionary proposal. Most master plans around the world are largely ignored (even in China). In Vietnam these plans are often referred to as “Hanging Plans,” suggesting that they often decorate the walls of planning departments but are rarely implemented. As in most countries, Vietnam line agencies typically make investment decisions based on their own population projects, rarely consistent with master plans, and often differing between agencies. Changing the planning process to be more in line with market dynamics would lead to better and more consistent development outcomes. Singapore and Hong Kong SAR, China are good examples of land use planning and internal consistency between spatial objectives and the provision of physical and social infrastructure.

### **HCCMP: Another Hanging Plan?**



*Source: Vietnam Urbanization Review 2012.*

### *Integrate land use and mobility planning*

When urban land and building regulations limit densities in urban areas, they push people and firms to the outskirts. As cities are forced to grow out instead of up, the urban transport network becomes increasingly important as the only way to connect people to jobs. A good transport system allows people to make efficient tradeoffs between the housing type and amenities they consume and the distance they travel to work. However, when the network is deficient, the problems stemming from stringent regulations in land markets are exacerbated. For example, people may be forced to live in slums close to job centers – often assuming natural hazard risks when they cannot afford to move into formal housing or cannot access cheaper land on the outskirts of cities because of a non-existent or inefficient urban transport system. In Santo Domingo, the capital of the Dominican Republic, 45 percent of the houses in the largest slum are located near a river and are flooded in heavy rains (Fay *et al.* 2003). Again, the poorest live in the lowest quality dwellings in the areas most at risk. Likewise, informal settlements in Rio de Janeiro or Caracas cling to steep slopes with large landslide risk during rainstorms. Publicly available information on hazard risk can enable households to make informed decisions (Box 3.3), but lack of coordinated land use and mobility improvements will force them to make suboptimal choices.

#### **Box 3.3: Publicly Accessible Information on Urban Hazard Risk Can Improve Household Decision Making**

Based on good information about hazard risk, households can make better decisions on how where to live, depending on the location's proximity to job centers, the quality and cost of transport services, and the location's risk of exposure to natural hazards. Some examples of such information systems include:

- The Bogota Disaster Vulnerability Reduction Project, launched in 2006, invested in information collection and vulnerability assessments for better targeting of risk reduction measures. One output was a database of earthquake vulnerability scores for all buildings in the city that helps prioritize upgrades and makes insurance markets more transparent (Prasad *et al.* 2009).
- Jakarta and Can Tho (Vietnam) recently carried out vulnerability assessments with World Bank support (World Bank 2012a). The studies demonstrate the use of geographically referenced data to pinpoint hazard risk and to support cost-benefit analysis of various risk reduction strategies. Flood-prone Jakarta, for instance, is considering measures such as drainage improvement, river improvement, upgrading of retention ponds, and various options for a coastal defense infrastructure.
- Better risk information supported the introduction of the Turkish Catastrophe Insurance Pool, a risk transfer mechanism set up after the Marmara earthquake in 1999 that killed at least 17,000 people and damaged 120,000 houses in the Istanbul region. The program reduced households' financial damages by enabling them to have catastrophic insurance and encouraging physical risk mitigation.
- A joint World Bank, Asian Development Bank, and Japan International Cooperation Agency study assessing future climate risks for coastal megacities found that by 2050, the frequency of major floods in Bangkok could fall from once every 50 years to once every 15 years. About a million inhabitants would be affected.

Thus, plans to connect neighborhoods should be integrated with plans for urban land use – especially density plans. For any of these policies to benefit the city as intended, they must be integrated throughout the planning process. However, urban transport is often an “institutional orphan,” with its responsibility often fragmented across agencies (World Bank 2013b). Land use planning is a core function of

development authorities, with transport planning often limited to developing the road network. Such fragmentation of responsibilities results in inefficiencies. In Bangalore, India, a new airport, several miles outside the city, was close to being commissioned when city authorities realized that the road connecting the city to the airport was inadequate.

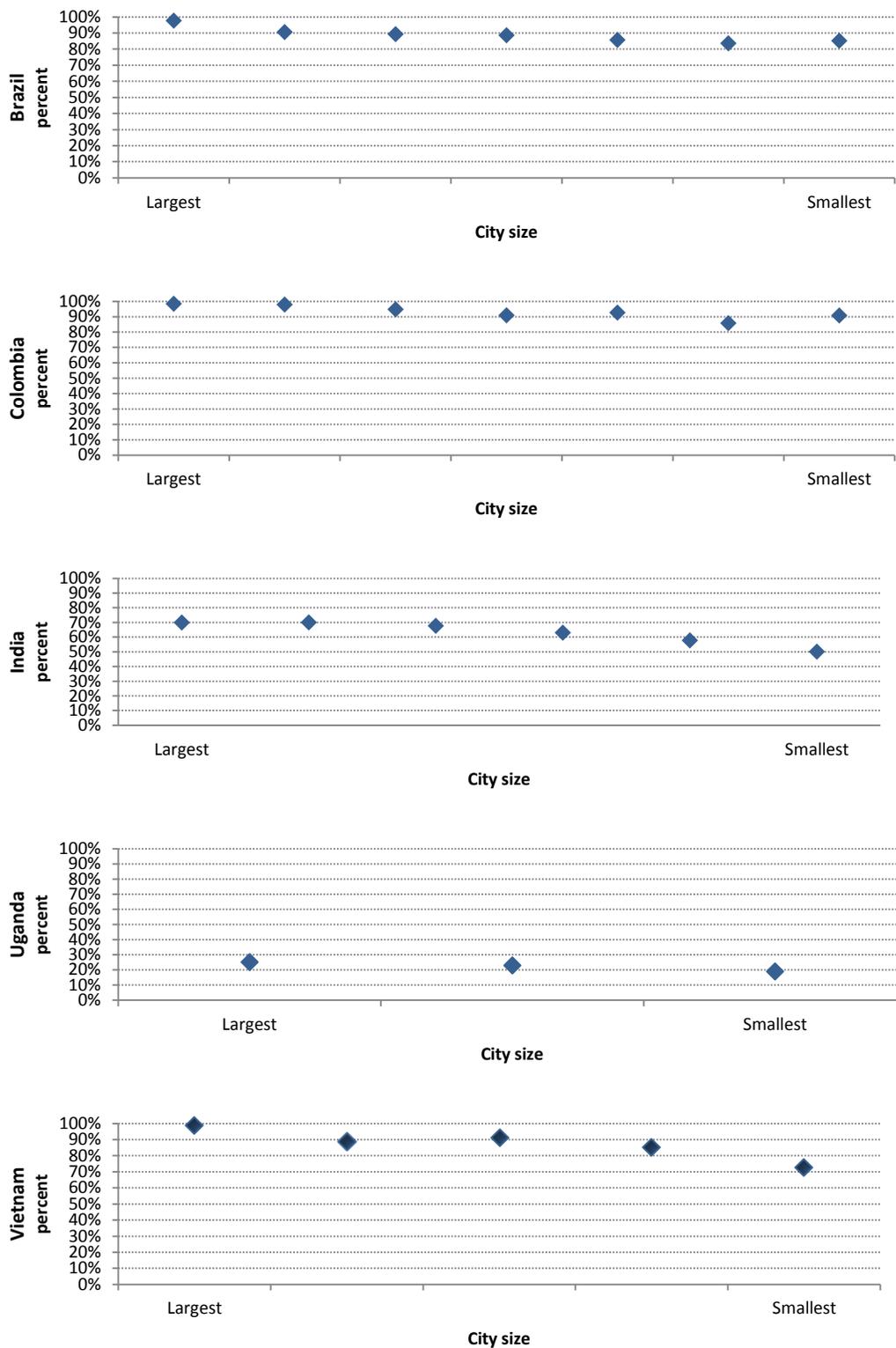
Land use planning is integral to transport planning because land use will largely determine transport demand. Different cities need different modal mixes, and different neighborhoods need different modes. Mass transport generally suits compact areas, private vehicles more sprawling ones. Mixed-use plans can reduce the need for long trips by locating housing, shops, services, and jobs all within a short radius. Studies also suggest that higher densities are good for efficiency and for environmental sustainability, reducing energy consumption and emissions by reducing vehicle miles traveled (Newman and Kenworthy 1989; Mokhtarian, Bagley and Salomon 1998; Schrank, Lomax and Eisele 2011).

Transport plans, in turn, shape land use by making specific sites more accessible. For example, a new road to undeveloped land can enable its development, or a new downtown metro connection can boost demand for redevelopment of the urban core.

### **Leverage competitive forces to expand services across urban and rural areas**

Consider Figure 3.5, which shows access to piped water for urban residents in Brazil, Colombia, India, Uganda, and Vietnam. In each of these five countries, water access varies with city size – but it does so differentially. In Vietnam, access is high but less equitable, with smaller cities showing lower access. In Brazil and Colombia, service coverage is high and fairly equitable. In India and Uganda, access is lower and less equitable.

**Figure 3.5: Share of population with access to piped water by country and across city size**



Sources: Brazil: IBGE 2000; Colombia: DANE 2005; Uganda: Uganda Bureau of Statistics 2010; Vietnam: General Statistics Office of Vietnam 2009; India: Ministry of Home Affairs 2001.

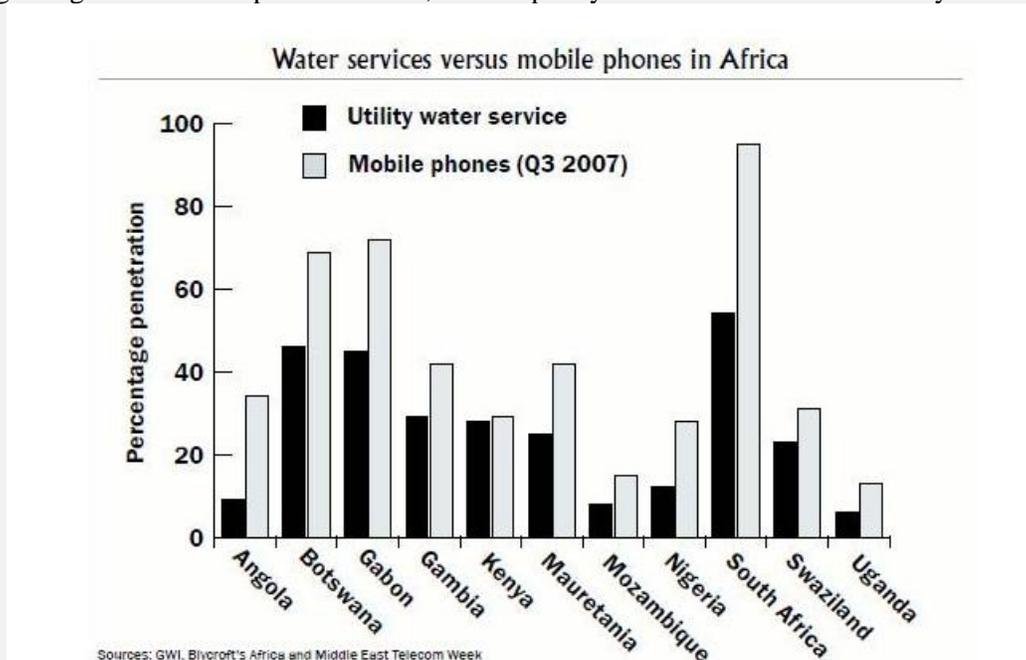
Beyond water supply, the lack of basic services such as electricity often forces households to tradeoff their health when they use alternate fuels for cooking and other uses. Indoor air pollution from solid fuels – wood, dung, coal, charcoal – continues to be widespread in areas where electricity is not available. This is a larger issue in rural areas, but is also still significant in urban settings. In Sub-Saharan Africa, for instance, 83 percent of rural versus 60 percent of urban households rely on solid fuels for cooking. Indoor combustion of solid fuels can cause severe health effects, especially among women and children who spend more time in the house (Bruce *et al.* 2000). These include lung cancer, pulmonary disease, low birth weight, cataracts, pneumonia, and tuberculosis. WHO estimates that exposure to solid fuel smoke causes 1.6 million deaths per year and the loss of 39 million disability-adjusted life years. With rising wealth in urban areas, households often switch to more convenient liquid fuels. For instance, kerosene use is widespread in urban areas where electricity access is lacking, especially where kerosene is subsidized, such as in India and Nepal. Perhaps as many as 500 million households globally still use fuels, mostly kerosene, for lighting, but also for cooking and heating. Apart from poisoning, fires, and explosions, kerosene poses risks from exposure to fine particulates, carbon monoxide, formaldehyde, and other potentially harmful emissions (Lam *et al.* 2012).

### ***Examine market structure***

When policy makers consider how to expand infrastructure and improve the provision of basic services, they have a choice. Rather than give first priority to financing, as is often done, they can look at the structure of markets for basic services and determine what rules will work best. In particular, policy makers may consider rules for competitive pricing and cost recovery. Indeed, in many cases the expectation of cost recovery through fees will determine the availability of financing (Box 3.4).

### Box 3.4: A Tale of Two Sectors – Expanding Access to Services

For the most clear-cut demonstration of the role of prices and price formation processes, consider access to water versus access to phone services in Sub-Saharan Africa: just about everywhere in Sub-Saharan Africa, access to mobile phones is greater than access to modern water systems. Official policy statements have been full of promises to enhance access to water for decades, yet similar statements have not been made regarding access to cell phones. Hence, official policy stance does not seem the key factor.



*Source: Global Water Intelligence 2008 Vol 9 Issue 5 May.*

Maybe *de facto* administrative capability is more important. Both water and phones need some level of regulation. Yet the regulation of modern phone systems is conceptually more challenging than the regulation of water systems. In all systems, regulation needs to set prices that cover costs. Costs and an allowed rate of return need to be calculated. So it is for water systems that typically have monopoly providers in any given area. The mobile phone sector has both competitive and non-competitive segments that require regulation. Multiple players pose challenges to regulating interconnection; as a result, telecommunications regulation should be more demanding than water regulation. However, many African countries have been able to provide a regulatory environment that enables penetration of mobile phone usage, even in challenging environments like the Democratic Republic of Congo, whereas they have not been able to achieve the same for water. Hence “capacity” to regulate does not seem to be the deciding factor either.

So what can explain the divergent patterns of access? A striking difference between the two sectors is the level of prices relative to cost. In the water sector, prices typically barely cover operating costs and tend to be about 30 percent of total cost. In the mobile telephone sector, prices tend to exceed cost. Unsurprisingly, both public and private system operators, who can charge and collect prices that exceed costs, have an incentive to expand systems and can do so. Providers who receive less than full cost have neither the incentive nor the financial ability to expand access.

*Source: Klein 2012.*

Recall Colombia's success in providing nearly universal access to water, electricity, and sanitation in cities nationwide (described earlier). A big part of Colombia's success is that policy reforms allowed fees to nearly cover costs. For example, average residential water fees more than doubled over 1990–2001 (World Bank 2004). With almost 90 percent of households having a metered connection, household consumption was nearly halved. And that, in turn, reduced the need to develop major new infrastructure. Even with fee increases, water remains fairly affordable in Colombia. The fee structure allows the government to cross-subsidize: richer households and industrial users pay for the poorest consumers. As a result, the average poor household spends less than 5 percent of its income on utility services.

Ugandan policy makers have started thinking about the rules that need to be in place to expand access to basic services. A water reform in 1998 focused on creating the right incentives for more efficient service provision, attributing responsibility to local service managers and increasing their accountability. Since 2000, the national government has been working with Uganda's National Water and Sewerage Corporation (NWSC) – autonomous public provider of water and sanitation to the country's large towns – to enforce performance contracts. Renewed every three years, the contracts include specific indicators that NWSC must meet at the end of the period (Banerjee and Morella 2011). However, Uganda's reform has not yet attempted to promote cost recovery through user fees. The NWSC charges a uniform fee across all towns and customer categories served. In 2010, of 23 areas served, only six covered production costs.

For some services such as urban transport, there need to be ways of regulating competition, as free market entry can undermine safety standards. The “penny wars” of Bogotá are an interesting example. Before a bus rapid transit system called TransMilenio was introduced in 2000, about 30,000-35,000 buses were operating in the city (Hook 2005). The government granted nonexclusive permits to the route operators, with whom bus owners were affiliated. The bus owners in turn charged their drivers fixed rents. The drivers' revenue thus depended directly on how many fares they collected. Cutthroat competition ensued, with unsafe results: drivers had a strong incentive to speed, cut people off, and carry too many passengers. The introduction of TransMilenio, together with a new regulatory framework, eliminated these “penny wars.” The new framework included bidding for all parts of the service, from routes to infrastructure. TransMilenio allocates the market to operators according to their quality, among other factors – and it pays them by the kilometer, assuring them of a certain amount regardless of their passenger load (World Bank 2013b).

Direct competition may also be technically unfeasible in sectors that naturally favor monopolies. Much of a city's networked infrastructure falls in this category: its duplication tends to be inefficient. A single network, fully built out, can often underbid any competitor (Klien 2012). Canada's cities are one example of a natural monopoly superseding market competition. Water utilities would at first compete to supply firms and households in a given market by laying separate pipelines. Then all the providers but one would fade away. In other cases, a monopoly provider started and was not challenged, either because competitors could not undercut it or because entry was forbidden by law. Natural monopolies can also appear in exclusive locations, such as airports and central metro stations.

Yet monopolies can abuse their market power, charging prices that are too high to be socially acceptable. Such prices can also make economies less productive and less competitive. So how can policy allow

prices to cover costs while ensuring that prices stay close to costs, as opposed to fattening a monopoly with excessive profits?

### ***Auctioning service franchises***

Regulation can closely mimic the effects of competitive pricing even where monopolies exist. City leaders can auction the right to provide a service for a certain period – moving away from a monopolistic price, and closer to that which would arise from competition. Firms that lose at auction exit the particular market. If it is possible to put such a monopoly franchise up for auction fairly frequently based on the lowest price, the auction will act like a market to set prices.

Many cities auction bus routes, assigning operators to predefined itineraries (e.g., Santiago, Bogotá, and London). Santiago awards five-year contracts using criteria that include the fare offered by the bidder, along with quality variables. Before the auctions, during a period of deregulation, bus fares had risen; with the auctions, the fares came back down. Where possible, franchise auctions repeated at intervals of one to three years can make price regulation essentially unnecessary. Such auctions have been used not only in bus transport but also in waste management. If a company loses a franchise, its assets – buses, garbage trucks – can be deployed elsewhere.

### ***Establishing subsidies***

Public policy can set service prices below cost-recovery levels to meet social and environmental obligations. When prices are set to cover all the costs of an infrastructure project, including the cost of capital, systems will likely be built out to serve all customers who are ready to pay the service cost. But policy makers may also want access to infrastructure to be extended to other customers, both for equity and for environmental sustainability. Price discrimination and subsidies can boost coverage and access.

### **Social equity**

The poor often pay higher prices per unit of, for example, water or energy than do wealthier people. Water vendors in poor urban areas may charge several times the unit cost of modern water service (Klien 2012). Price discrimination is a way to restore equity by charging rich people more and poor people less. One method of price discrimination is to offer the poor a specially tailored price-quality mix. For example, poor people who can afford to buy water at times – but not regularly – can do so by the bucket. Or the poor can be served by simpler pipelines. In other ways, too, the poor can be offered flexible service that is better than what they had before, yet not exactly what the rich receive. (Water that is not fully treated can still serve many common uses, such as flushing toilets. Poor people can make their water potable by boiling it.) Finally, the poor can be given more flexible payment terms; for example, through the use of electronic cards. In pursuing these possibilities, it can help to let unconventional providers – from for-profit vendors to community-based organizations – enter the market (Baker 2009). While these are clearly not the only solutions for improving access to water, they provide various second-best options to provide services of varying quality.

Governments can also provide subsidies for equity. However, one must recognize that many subsidies do not increase access to services. For example, subsidizing an existing utility may help the better-off people who are already connected, but no one else (Komives *et al.* 2005; Estache and Ginés de Rus 2000). Accordingly, policy makers should focus discussions of subsidies on policies to expand access. They should target subsidies to poor people, either by conducting means-testing (as in Chile's water subsidy system), by targeting areas where the poor tend to live, or by offering lifeline rates (for reduced service at

a reduced price). Lifeline rates raise an objection, though: they can benefit people at any income level. Such objections are a reminder that subsidies require careful design. Basing them on quantity or consumption does not necessarily promote equity. A study of 26 quantity-based subsidy cases in Asia, Africa, and Latin America suggested that 24 were regressive, and that where coverage is not universal, connection subsidies may be better at reaching the poor (Komives *et al.* 2005). A noteworthy innovation in enhancing access to services for the urban poor is through Output-Based Aid (OBA), which links the payment of public funds or subsidies to the achievement of specified outputs and actual service performance (see Box 3.5).

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### **Box 3.5: Using Output-Based Aid in Urban Projects**

The people most affected by the lack of access to basic services in urban areas are the poor, who often obtain essential services like drinking water or electricity from informal vendors at substandard quality and at a high premium. Given the growing demand for basic services, there is an increasing need to improve service delivery in low-income urban settlements. One way to help the urban poor gain access to basic services is output-based aid (OBA), which links the payment of public funds or subsidies to the achievement of specified outputs and actual service performance. Output definitions are designed to be as close to the desired development outcomes as is practicable, and within the scope of the service provider to deliver. Most urban OBA projects also require that a portion of the subsidy payment be withheld until sustainable service delivery has been demonstrated.

**Targeting the urban poor:** A core component of OBA is explicit targeting of low-income households. For the urban poor, a major hurdle to obtaining basic services is the high initial cost of access, such as a connection fee for water supply. OBA can help reduce this barrier by paying a subsidy to bridge the gap between the actual cost of access and what users are willing and able to pay. Geographic targeting can be effective in cities where poor households tend to be concentrated in slums and informal communities; alternative targeting strategies subsidize only those services that the non-poor are less likely to use, or target beneficiaries based on their income or poverty level.

**Risk transfer and access to finance:** In OBA schemes, payment on delivery of specific outputs shifts performance risk to service providers, which can be public, private, or NGOs. Since service providers are not paid the subsidy in full until they deliver outputs, they must have access to sufficient finance for the initial investments, a significant risk and one of the biggest constraints to developing output- or results-based projects. When service providers cannot afford to finance the whole project in advance, phased subsidy payments against intermediate outputs have been used. On rare occasions, small advance payments have been required for start-up costs and awareness campaigns. Most service providers meet pre-financing needs from internal cash flows or externally sourced funds, or both.

**Designing OBA projects for the urban poor:** A major obstacle to service provision in informal or slum settings is the often precarious tenure status of slum dwellers; many are ineligible for formal household connections by law. Residents also have no guarantee that their dwellings will be safe from demolition. Service providers may lack legal or regulatory authority to serve these informal areas and are also likely to lack incentives to do so for fear of low uptake or because they see it as a high risk investment. For OBA schemes to succeed, they must have buy-in and commitment from local governments. Furthermore, the government agency should have the administrative capacity to manage OBA contracts and subsidies.

**Lessons learned and prospects for scaling-up or replication:** Although OBA is not the solution for all urban service problems, it is a tool to help increase the access of urban poor households to basic services, particularly where the cost of service access is unaffordable, and where service access needs to be built into urban project design. Land tenure issues must be addressed early on in the design stage. Active outreach and engagement with community-based organizations and political and community leaders is also key for successful project design and implementation. Incorporating OBA schemes into broader urban reform and slum upgrading programs can also be effective as they can bring multiple stakeholders together, acting as a resource convener, and potentially play an important role in shaping the policy framework for urban development in terms of service provision and service access for the urban poor.

*Source:* Adapted from Ahmed and Menzies 2012.

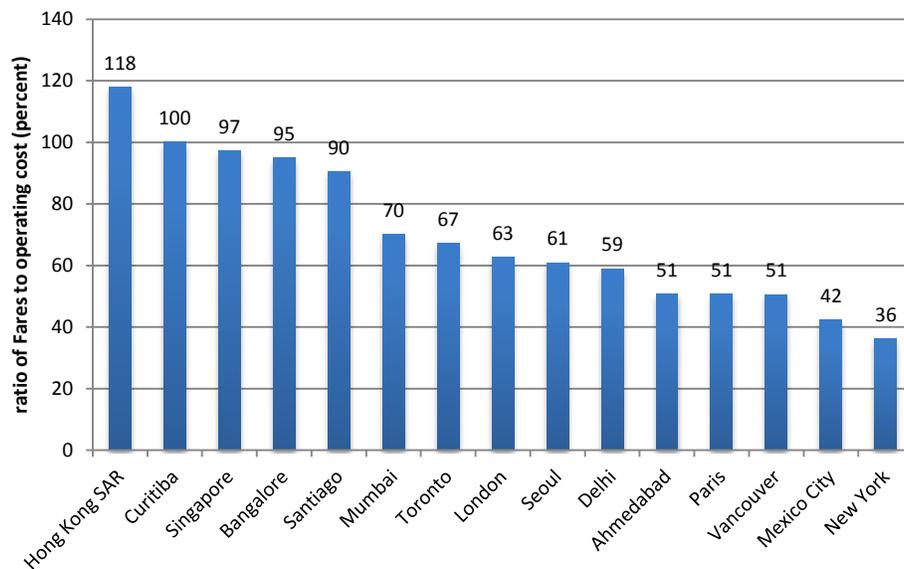
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### Environmental sustainability

Public transport can mitigate urban congestion: a bus carrying 40 or 50 people takes up no more road space than two or three private cars. And public transport pollutes less, generating fewer greenhouse emissions. Yet in many countries, public transport is unaffordable for the poor. For example, households in Kampala, Uganda, pay US\$13 a month on fares, about 8 percent of their budget (World Bank 2012c). Although that is consistent with global estimates of what people pay for transport, it is unaffordable for the poor. To use public transport, the poorest 20 percent of households would need to spend 41 percent of their income on fares. Similar patterns appear in other cities worldwide.

The predictable result is that in many developing countries, urban public transport ridership is low. In cities where transport fares do not cover the full cost of service provision, transport subsidies can boost ridership. But to succeed, such subsidies require strong contractual agreements and regulation. The problem is that even after fares are decoupled from full operating costs, transport providers still need assurance that their costs will be met by revenues. Cities such as Seoul, Curitiba (Brazil), London, and Bogotá have solved the problem with gross cost contracts, which assure operators that their revenues will be based on performance, not on fare box collections (or not directly so). To cover costs fully, public agencies then seek other sources of revenue. Transport systems around the world vary widely in the share of operating costs recovered through fares. In a sample of 20 public transit systems, only five fully covered their costs through fares. In New York, 55 percent of costs were recovered through fares; in Moscow, 11 percent (Figure 3.6).

**Figure 3.6: Ratio of public transit fares to operating costs in a selection of the world’s largest cities**



*Note:* The numbers in this chart relate to bus and metro systems operated by public entities or large corporate entities. A weighted average was based on ridership across modes. Small private operators were not included because data were lacking.  
*Source:* World Bank 2013b.

### Connecting cities

Connections – between and within cities – benefit producers and consumers, both in urban and rural areas. They give producers access to input (including labor) and output markets. They give consumers

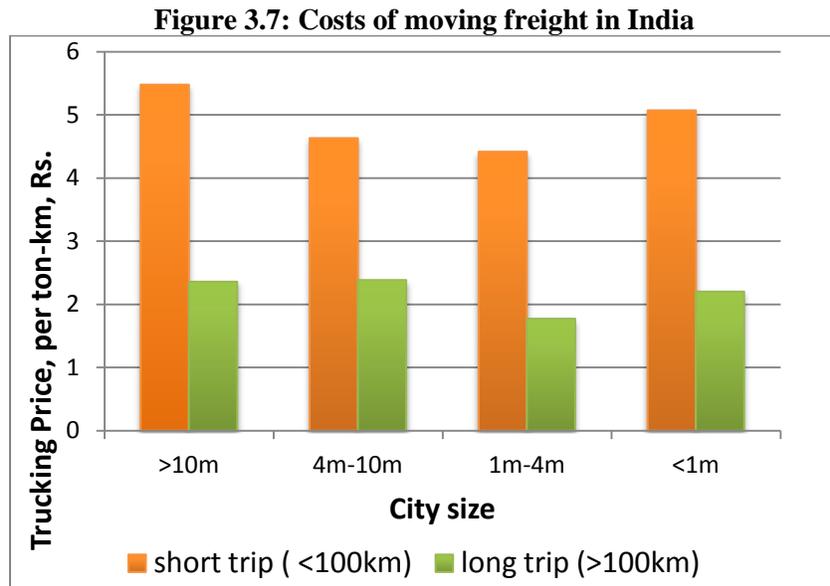
options and, in many cases, better prices. And connections expose cities and rural areas to new economic opportunities. But policy makers who envision better transport connections for cities and neighborhoods face difficult choices. With limited resources, they cannot invest in everything. It is hard to know which new or improved connections will yield the highest returns over time.

Setting priorities for connective investment means picking winners and losers in the short run – but in the long run, thinking about priorities can make a vast difference for cities, surrounding rural areas, and even countries. To identify the most effective additions and improvements to the networks connecting cities and neighborhoods, policy makers can take the steps described in the following three subsections.

### Value the city’s external and internal connections

For external connections to other cities and rural areas, policy makers can compare transport costs – and the density, quality, and capacity of roads, railways, waterways, and the like – with data from similar places. In this way, they can determine where improvement is most needed.

Systematically disaggregating transport costs can identify bottlenecks and reveal opportunities for infrastructure improvement to yield high dividends. A survey of truckers in India showed that transport costs were highest near large cities and their surrounding rural and peri-urban areas, a pattern similar to that found in Vietnam and Brazil. Freight rates for metropolitan transport in India, defined as trips shorter than 100 kilometers, averaged as high as Rs. 5.2 per ton-kilometer (US\$0.12) – twice the national average of Rs. 2.6, and more than five times the cost of such trips in the U.S. (Figure 3.7).



Source: World Bank 2013a.

Why are India’s metropolitan freight transport costs so much higher than its long-haul costs? One reason is the use of smaller, older trucks on metropolitan routes. Another is the higher share of empty backhauls (truckers returning without a load) on metropolitan routes. Finally, trucks on metropolitan routes clock about 25,000 kilometers annually – just a fourth of what they need to be economically viable. To improve coordination and reduce the cost of metropolitan freight movements, trucking firms could adopt logistics management systems; they could collaborate or consolidate with competitors; or they could form trucking associations. If India’s high freight costs are not reined in, then they will affect national economic

development, as experienced in Vietnam. That is because both nations have large concentrations of economic activity in and around metropolitan areas.

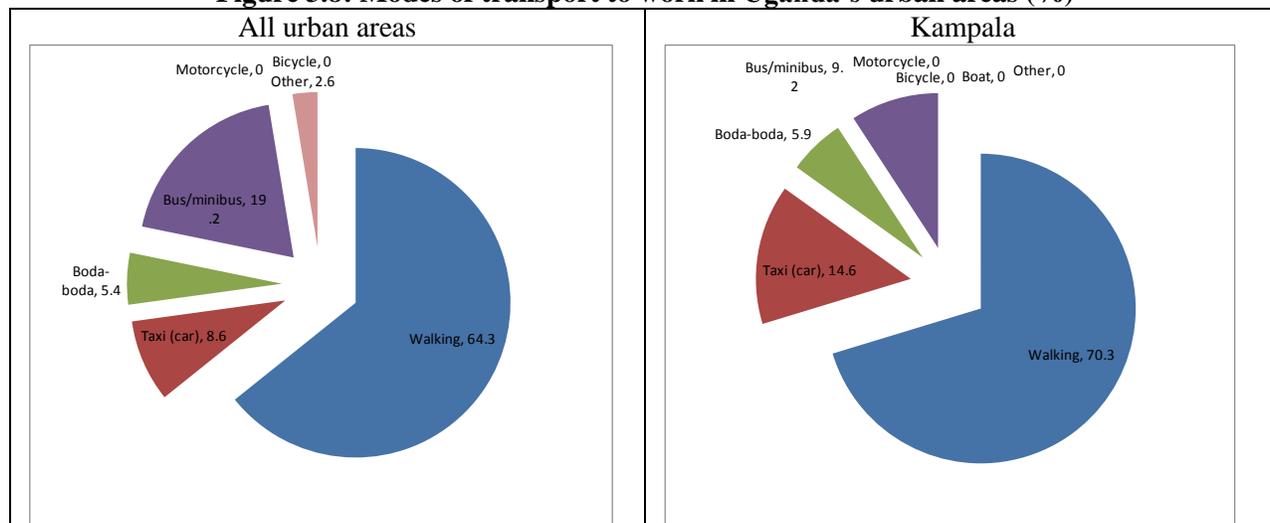
Alternatively, policy makers can identify possible transport cost reductions and connectivity gains that reflect the city's desired mix of economic activities and extent of specialization. In Colombia, lowering transport costs along the country's key trade corridors can enhance competitiveness for its cities and for the nation. For example, transporting freight by road from Bogotá to the Atlantic costs about US\$94 per ton while maritime transport from the Colombian coast to the U.S. is less, at about US\$75 per ton. High domestic transport costs undermine the competitiveness of goods produced in Colombia's largest cities, especially compared with other large cities around the world. Reducing domestic transport costs by 12 percent can lead to an increase in exports of about 9 percent (Boyle 2010).

For internal connections that link people with jobs, it is important to identify the problems: Are gridlocks and lack of adequate public transport deterring residents from working outside their immediate neighborhoods (making labor markets inefficient)? Conversely, are long commuting times or high fares forcing residents to live in crowded slums so that they can walk to work? A city that faces one or both of these challenges needs a plan for a better transport system, including a desired mix of transportation modes. The plan must balance two main objectives: increasing the supply of affordable transport options and ensuring that congestion and pollution remain within acceptable limits.

### **Coordinate among transport options and with land use**

As discussed under the Planning section, policy makers must systematically coordinate transport plans with land use policies and related infrastructure plans. Although each situation is unique, it is important to ensure that transport options are consistent with affordability. In Uganda for example, public transport is unaffordable to many at current income levels. Household survey data suggest that 64 percent of urban dwellers walk to work, and walking trips are as high as 70 percent in Kampala (Figure 3.8). As cities in Uganda are expanding their spatial footprints, the limited reach of walking trips severely limits labor market opportunities for people who live further away from economic centers, and may even exacerbate slum formation, as many people will trade off housing quality to be close to jobs.

**Figure 3.8: Modes of transport to work in Uganda's urban areas (%)**



Source: Uganda Shared Growth Report 2012.

Typically, transport choice is determined by income, with the mode and number of trips increasing with income. In Addis Ababa, 70 percent of trips are by walking and public transport is estimated to cost 3-37 percent of household income, with an average distance walked of 5 kilometers. In Nairobi, it is 4 kilometers, where 48 percent of trips are by non-motorized transport, including walking – and the poor pay 34 percent of their income on transport. And in Dar es Salaam, the average distance walked is 2.2 kilometers and the share of non-motorized transport is 45 percent, with transport expenditures for the poor accounting for 53 percent of income (Sub-Saharan Africa Transport Policy Program (SSATP) 2002; Africa Infrastructure Country Diagnostic (AICD) 2008). This is consistent with the situation in many African cities (AICD 2008). This implies that at low income levels, the wider availability of different service levels and modes at different prices is a useful strategy for provision of urban transport services. And a challenge here is that although most (poor) people walk, hardly any facilities and safety standards are available to protect pedestrian road users. Improving sidewalks, streetlights, and other measures to protect pedestrian users should be important in an urban transport strategy. In the short term, it appears to be useful to complement public transport with a wide range of service levels and modes at different prices, supported by investments to reduce pedestrian fatalities.

Policy makers can encourage the use of public transport and increase the geographic scope of the labor market, however. In Brazil, the government requires formal sector employers to provide transit tickets to their employees through a system called *vale transporte* (VT); firms then deduct the VT expenditures from taxable income. The VT system – albeit affecting only the formal sector – effectively spreads the cost of transport subsidies between employers and the government.

In most rapidly growing cities, a useful mobility plan needs to make way for multiple options for shared travel. Metro rail systems and bus systems are the most common among them. There may also be multiple operators managing each of these systems. It is important that these are well coordinated and feed into each other rather than duplicate each other. Therefore, an important regulatory role will be to coordinate service planning.

## Leverage investments that will yield the highest returns for cities – collectively and individually

National leaders must identify the most efficient investments in connections among all the cities in a country. Where is demand highest for the expansion of intercity infrastructure and transport services? Which corridors are identified through spatial analysis and simulations as most central to the network, such that improving them will yield the highest returns for efficiency and equity? Similarly, leaders must find ways to make transport within cities affordable while limiting congestion and pollution. This is particularly important for infrastructure such as roads, where user charges alone cannot recover costs (Box 3.6). Investments to increase capacity should be combined and aligned with other policies. Targeted subsidies, though not effective for all purposes or in all contexts, can sometimes be used to make transport more efficient as well as more equitable and safer for the environment. And other fiscal and regulatory tools can be used to manage demand for particular transport modes.

### **Box 3.6: Pricing and Funding Through Ancillary Services**

A number of infrastructure services cannot be charged for easily. Roads are a prime example. Here it may be possible to use ancillary services to provide revenues for the venture. For example, a toll road franchise may be combined with the right to let service concessions for gas stations as well as restaurant or hotel services at rest stops along the highway. Going further, it is possible to provide a toll road company with rights to real estate development along parts, or all, of the highway. When granting a highway concession, the full package of rights and obligations can be auctioned so as to obtain the best price for the whole package. Airport franchises are an example of this, where the rights to concession services (shops, restaurants, etc.) at the airport are a major source of revenue.

Such add-ons to the basic infrastructure service can make funding possible, while avoiding recourse to the regular government budget. This is a way to make an infrastructure service independent of fiscal processes and can help insulate the service provider from undue political influence.

At the same time, there is danger of excessive subsidization. Economically unviable projects may be rendered possible by providing enough support of this type. Hence, cost-benefit analysis should routinely be used to ascertain that the infrastructure service is likely to be welfare enhancing.

## Financing cities

Having identified priorities for planning and connecting, policy makers confront the problem of financing those investments. The main difficulty is the need for money up front. Large capital outlays are needed to provide infrastructure and services that are not fully in demand now, but will become so as urbanization picks up speed (Mohan 2009). The large capital investments that are needed in the construction phase – whether for transport, water provision, solid waste management, or sewage removal and treatment – are likely to far exceed the budget of any city government. But financing can become more sustainable through taxes realized with increased economic growth, and with the ability of policy makers to leverage land markets and approach local currency debt markets.

How do policy makers bridge the gap between readily available resources and investment needs? What sources should they tap? To start with, the government can establish its creditworthiness by first securing cash flows from user fees and taxes and by leveraging the value of land in several ways, including taxes.

Only after that can the government begin to borrow money and attract private investment, making finance easier. Whether financing is public or private generally does not make the difference between successful and struggling cities. But there are at least two situations in which private financing may be the preferred course: when the government sees PPPs as a way to improve efficiency in service provision, and when the government suffers from severe credit constraints that prevent it from obtaining credit for improvements to publicly run systems.

### Value and develop creditworthiness

Without domestic credit markets, and often lacking the transparency needed in municipal bond markets, many city governments in developing countries cannot access long-term credit. Experience shows that subnational debt can work if clear regulations are in place to:

- Guide the issuance of debt;
- Manage risks from borrowing; and
- Clearly set forth the conditions for subnational governments to issue debt (including the purpose, type, and amount of debt that can be issued).<sup>46</sup>

To make the issuance of debt to cities more transparent, Colombia has published traffic light ratings of local government payment capacity, with red, green, and yellow signals reflecting a combination of liquidity and solvency indicators. To rate municipalities' subnational debt, a red light identifies those whose ratio of interest to operational savings exceeds 40 percent and whose ratio of debt stock to current revenues exceeds 80 percent. Red-light municipalities cannot borrow. Green-light municipalities can. Yellow-light municipalities can borrow only after obtaining the approval of the central government.

Creditworthiness is limited not only to local governments – it extends to their utility companies. In Kenya, the Water Services Regulatory Board calculated and published utility shadow credit ratings for 43 water service providers in 2011 and found only 13 providers to have investment grade ratings.

Smaller cities can seek short- and medium-term loans from higher levels of government and pool their credit. Thus, governments of smaller cities can use bond banks, loan pools, and guarantees to reduce lenders' risks. There are two common types of municipal bonds: general obligation bonds – debt instruments secured by general purpose municipal revenue such as property taxes – and revenue bonds – debt instruments secured by the revenue generated from specific municipal assets (such as ports, toll roads, and water and wastewater utilities), with or without recourse to general revenues. Revenue bonds are particularly useful in cases where bond markets are not well developed. Colombia, India, Malaysia, Romania, the Russian Federation, the Slovak Republic, Slovenia, South Africa, and the República Bolivariana de Venezuela provide examples of countries where cities have raised funds from municipal bonds.

In the absence of a well-developed bond market, financial intermediaries in diverse forms play important roles in mobilizing resources for urban infrastructure financing. In Colombia, a successful financial intermediary is FINDETER (Financiadora de Desarrollo Territorial S.A.), a government company created to finance regional urban infrastructure projects. More than 90 percent owned by the national government, with the remainder owned by the regions (Departments), FINDETER provides resources for financial

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<sup>46</sup> This includes national government clearing of subnational borrowing.

intermediaries who assign them to regional authorities. It has received funds from multilateral banks and has consistently received high credit ratings (World Bank 2011a). Still, none of these methods can replace a creditworthy local government.

### **Coordinate public and private finance using clear and consistent rules**

When city governments have constrained access to credit, private investors may step in to fill the gap. There are many types of partnership structures, with each one transferring different levels of risk to the private sector. They include service contracts, management contracts, leases, and privatization. Under any of these structures, property rights must first be clearly defined so that creditors need not depend on the government's promises. Then a PPP, with private sector selection mechanisms based on the market and on cost-benefit analyses, can improve project selection and ensure project sustainability while adding sources of infrastructure financing. Nevertheless, PPPs are no magic bullet: they require commitments to sustainable cost-covering tariffs or equivalent tax revenues. They cannot stand in for good financial management or good project evaluation. Clear rules must dictate the procedures, the requirements, the approvals, the institutional responsibilities of the entities involved, and the allocation of risk.

Consider Ghana, where such rules were not in place. In 2002, the Government of Ghana initiated a process to encourage PPPs in the urban water sector. However, lack of transparency and accusations of corruption in the selection process led to the end of the PPP. In contrast, Chile put in place a clear and transparent procurement process, focusing on public awareness and a learning-by-doing approach that allowed for adjustments along the way. This process led to the award of 21 road projects on a competitive basis between 1993 and 2001 (Hodge 2006). The bidding started with smaller projects to test the market while also minimizing the risk for the private sector. More than 40 Chilean and international companies from 10 countries participated in the bidding through 27 consortia.

To successfully implement PPPs, city leaders will have to consider strengthening public sector capacity, laying out the appropriate legal and sector framework, promoting rigorous planning and risk assessment through feasibility studies, ensuring transparent and competitive procurement, building strong monitoring systems, and allowing flexibility for adapting to unpredictable events.

### **Leverage existing assets to develop new ones, linking both to land use planning**

Land sales and leaseholds can provide initial capital for new infrastructure investments. Sales in Cairo, Istanbul, and Mumbai provide examples of the revenue potential of land auctions. For example:

- In Cairo in 2007, the auction of 3,100 hectares of desert land for a new town generated US\$3.12 billion – an amount 117 times greater than the country's total urban property tax collections, and about a tenth of the size of national government revenue. The proceeds were to be used to reimburse the costs of internal infrastructure and to build a connecting highway to Cairo's ring road.
- In Mumbai in 2006-07, the auction of 13 hectares of land in the new financial center – Bandra-Kurla Complex – generated US\$1.2 billion. That was more than 10 times the total 2005 fiscal spending of the Mumbai Metropolitan Regional Development Authority, and six times the total value of municipal bonds issued by all urban local bodies and local utilities in India in more than a decade. The proceeds were to be used primarily in financing projects identified by the Metropolitan Transportation Plan.

- In Istanbul in 2007, the auction of an old bus station and government building generated US\$1.5 billion – more than the city’s total 2005 fiscal expenditures and infrastructure investments.<sup>47</sup>

Yet policy makers should recognize that all successful land-based financing instruments require at least three kinds of rules to be in place. First are rules to assign and protect property rights. Second are institutions for the valuation and public dissemination of land values across various uses. Third is a strong legal framework, with a healthy judicial system to handle disputes and oversee the land-based financing process. Furthermore, a single planning strategy should integrate land-based financing with urban land use planning.

However, by first developing land management institutions, identifying the infrastructure needs, and integrating planning across sectors, financing will follow as investors will be able to better assess risks and see the city as a good investment.

### **Managing the implications coming from different forms of decentralization**

More generally, the financing of all local services is challenging. While services are best delivered locally, the local tax base is often narrow. That is true not only for cities, but for all subnational governments (SNGs).<sup>48</sup> All poverty is “local”—and given their proximity to citizens, SNGs are often better suited than higher levels of government in addressing these challenges. First of all, they can be more efficient in detecting citizens’ needs given their informational advantage. This is particularly relevant for beneficiary identification in poverty programs. SNGs can direct resources towards these needs (*allocative efficiency*) and can provide some services more efficiently than higher levels of government (*productive efficiency*). Also, political decentralization lowers the “barriers to entry” for different groups of society, so they can more easily and directly participate in decision making (Box 3.7).

For a poverty effort, it is critical that the net fiscal incidence remains pro poor.<sup>49</sup> That is, regressivity of local revenue can be accepted as long as expenditures are progressive and lead to an overall positive incidence. But it is also clear that one must consider the burden and benefit distribution of the tax system and public expenditures as a whole—and this requires coordination across all levels of government. But achieving this is becoming harder in the current urban and rural dynamics—in fact, it represents one of the challenges to achieving the MDG targets. As urbanization unfolds, the more populous areas acquire higher fiscal capacity. This implies they have more resources available to address poverty issues, either through taxation or expenditures. Absent any convergence effect, SNGs in rural areas will face continued or even higher resource constraints. But given that poverty is concentrated in these areas, there is an increasing gap between needs and the means to address them.

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<sup>47</sup> This property in Turkey was purchased by Sama Dubai with grand plans to build the Dubai Towers in Istanbul – to be the tallest skyscrapers in Turkey. However, the municipality and developer could not come to terms on the impact of the buildings on the surrounding area so the project has been halted indefinitely. Meanwhile, the land remains undeveloped.

<sup>48</sup> The term “subnational governments” encompasses, among others entities, regional or state governments, provinces, and municipalities.

<sup>49</sup> Refer to Boex *et al.* (2006).

### **Box 3.7: Key Design Issues of Decentralization**

The three elements of decentralization are administrative, fiscal, and political: (i) administrative decentralization relates to expenditures and services assigned to subnational governments; (ii) fiscal decentralization is related to subnational own revenue, transfers, and debt; and (iii) political decentralization refers to elections and the delegation of authority, as well as citizen participation.

Countries are constantly adjusting and fine-tuning their intergovernmental relations. Given the several trade-offs which have to be faced, the three elements of political, expenditure and revenue decentralization constitute a never-ending balancing act. In fact, decentralization is a “moving target” – there is no final model that countries can reach. What matters most is to fit the different design elements together coherently and avoid disjointed decision making.

The degree of fiscal, political and administrative decentralization is not related to whether a country is federal or unitary. Relevant examples include unitary China, with about 70 percent of expenditure decentralization (accountability, in turn, is upwards towards the central level). In contrast, in federal Mexico, the degree of expenditure decentralization is about 30 percent.

In any decentralized system, there are also other trade-offs to be faced. Revenue decentralization reduces the ability of central governments (or “senior levels”<sup>50</sup>) to redistribute: they lose their ability and room to maneuver. Expenditure decentralization implies that priority setting needs to be done in a coordinated fashion among the different levels. This can affect the capacity to establish a “level playing field” in countries through fiscal equalization. Agreeing on an appropriate level of equalization becomes harder each time.

There are also other risks: institutional capacity can be weak; there can be capture of entities; and the inclusion of the poor and their priorities cannot be taken for granted. It is also clear that party systems and electoral rules influence greatly the service delivery priorities of councilors, mayors, and governors, so it cannot be taken for granted that services and resources are directed where the needs are greatest. Urban areas are in principle more attractive for “vote-seekers” than rural areas, and this can create an undesirable expenditure bias.

Weighing the risks and advantages of SNG is prudent—but countries often have no choice: several levels of government need to find ways of cooperation to address the MDG challenge, and this has different connotations in rural and urban areas.

It is clear that not all of the undesirable effects of urban and rural dynamics can be addressed through SNGs. A range of policies and other interventions need to be in place and steered and implemented in parallel with national governments. But many examples from across the world underscore that not only can effective policies be crafted, but they also rely increasingly on responses in an intergovernmental fashion.

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<sup>50</sup> Some transfers are managed from subnational tiers to their lower tiers (often municipalities).

Overall, the need for asymmetric arrangements<sup>51</sup> increases as these allow different territorial entities to acquire different levels of autonomy so they can more effectively tailor responses to specific needs. But it is also clear that asymmetry is an imperfect policy, as urban and rural service delivery gaps may not coincide with territorial boundaries. The tensions that can arise from asymmetry are inherent to urban-rural dynamics and the trade-offs need to be addressed to enhance the MDG impact of subnational interventions.

### **The financing challenge of the MDGs in rural areas**

SNGs face a formidable challenge: they host the growing number of the poor, but under growing disparities in fiscal capacity, they are increasingly resource constrained. This adds considerably to the challenge of providing services to citizens most in need.

Due to their limited fiscal capacity, SNGs in rural areas are more dependent on transfers from higher levels of government.<sup>52</sup> Dual economies and informality may further limit subnational taxation. Some rural governments can even be in a “transfer dependence trap,” as there is no linear relation between increased tax effort and the level of expenditures that can be achieved—a dilemma that constitutes one of the “dangers” of decentralization.<sup>53</sup> Transfer dependence is particularly large for regional governments in many unitary governments (e.g., Bangladesh and Bolivia), as tax bases that are suitable for regional management (automobile taxes, for instance) have been given to municipalities. This has been a perennial sequencing problem of decentralization. For SNGs in rural areas, there are therefore limited possibilities to engage in redistribution through local taxation.<sup>54</sup>

Redistribution therefore mainly needs to come from the expenditure side. But this depends critically on the level of expenditure decentralization. More often than not, these SNGs do manage only parts of the service delivery: public investment and infrastructure. Human resource management, particularly in the social sectors (health and teaching personnel) has long been a politically sensitive area and most management decisions remain centralized in many countries. On the other hand, situations of clientelism can lead to excessive staff rotation and undermine capacity even further. Taken together, this can lead to disjointed management and decision making.

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<sup>51</sup> Two countries that have formally adopted asymmetric treatment are Spain (during the 1980s) and Italy (in the 2000s).

<sup>52</sup> That potentially buoyant tax revenue is also being used by SNGs in rural areas is highlighted by some examples in the OECD; for example, local income taxes are used in countries with dispersed populations (e.g., Sweden, Finland, and Norway).

<sup>53</sup> This insight is based on Prud'homme (1995) who cited this as one of the “dangers” of decentralization. Assume a SNG whose total revenue is composed of 10 percent in taxes and 90 percent in transfers. All other things equal, financing a 10 percent increase in expenditures requires doubling the tax effort. This often exceeds the institutional capacity and willingness to assume the political cost.

<sup>54</sup> The property tax can establish differential rates (e.g., agricultural land is often taxed at a lower rate than urban land), but overall the revenue is inelastic and has high administration costs. The sales tax, if applied, is levied on high-income and low-income groups, and is therefore regressive; however, it does achieve a closer link between consumers of services and payment for them (compared to income tax, for instance). Potentially there could be piggy-backing on a national tax (income tax or sales tax of higher level, for instance), but once differential rates are applied, the administration becomes very complex, and the issue of the mobility of the tax base arises; in this respect, a sales tax is better suited for piggy-backing due to lack of mobility.

Given these uneven advances and levels of autonomy in expenditures, SNGs in rural areas are constrained in their ability to provide packages of services to the poor and to target the incidence of spending such that services are directed where the needs are greatest.

In addition, the often low population density implies higher per capita costs in providing public services.<sup>55</sup> Consider that:

- The marginal cost in service provision for water and sewage increases substantially in rural areas, and it is particularly high for secondary and tertiary health care.
- Education costs for primary and secondary education are often less affected by economies of scale than other services, but there are thresholds beyond which costs can increase substantially also in rural areas.<sup>56</sup>
- Roads, in turn, can facilitate access to economic centers, but given the limited possibility to establish user fees and toll roads, financing by other entities or higher levels of government is required.

These challenges have important consequences. They require different levels of governments and entities to contribute with grant financing and service delivery. These coordination requirements can be particularly significant at the regional or intermediate level of government.<sup>57</sup> Investment funds play a large role in rural areas as they co-finance or execute public works directly. Some of these entities have been trying to substitute for weak institutional capacity. But this has also led to a bypassing of rural SNGs in service provision, creating an undesirable spiral of weak accountability and capacity.

### **The financing challenge of the MDGs in metropolitan areas**

In contrast to rural areas, SNGs in urban areas have higher fiscal capacity and hence can influence outcomes much more through their own revenue decisions.<sup>58</sup> Absent any convergence effects, fiscal capacity in these areas will increase as agglomeration unfolds. The tax incidence of such revenue decisions naturally depends on the particular taxes and user fees applied. Common revenue sources are: (i) land-related revenue (e.g., property tax, improvement levies, auctions, leases), which can affect the locational decisions and income of individuals; (ii) the personal income tax (applied at the local level in 13 of 27 OECD countries); and (iii) user fees, which are usually applied at uniform rates and therefore can have a regressive effect.

But there are several stumbling blocks which can limit effective tax decisions in urban areas, and can also affect fiscal equalization more broadly. One of these is the governance arrangements in metropolitan areas. Two models have emerged: (i) single-tier models; and (ii) two-tier models, which are more

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<sup>55</sup> For further reference on service delivery and equalization issues in rural areas refer to: Hon (2009); Kitchen (2006); McMillan (2007).

<sup>56</sup> Costs increase at a very small class size. Otherwise, economies of scale are limited, and except for special grants and incentives for teachers to move to rural areas, there is no additional cost.

<sup>57</sup> Authorities can be delegated or elected; in some cases there are dual authorities (e.g., in Latin American countries, among them Bolivia and Ecuador). Some of these entities can be solely responsible for rural areas.

<sup>58</sup> Nevertheless the overall level of transfer dependence of metropolitan governments can be substantial. Some of the more financially autonomous metro areas include Addis Ababa, Pretoria, and Melbourne (Shah 2012). In turn, cities like London, Berlin, and Bucharest are dependent on central grants for about 80 percent of their revenue.

frequent and require vertical<sup>59</sup> and horizontal<sup>60</sup> coordination. However institutional changes often cannot keep up with rapid demographic changes and so usually remain informal. It is no surprise then that many of these are mere planning entities with no taxing powers, or that central government influence is considerable. This also affects if and how citizens are represented and can make their voice heard (Box 3.8). This has three consequences:

- It rules out more firmly establishing the authority to tax at these levels which can be used to finance local expenditures.
- It limits possibilities for redistributing within metro areas or to other subnational units,<sup>61</sup> which is critical for maintaining a “level playing field” for all entities.
- If revenues are further decentralized in urban areas, it can undermine the capacity of the central government to redistribute to other areas, among them the rural SNGs.

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<sup>59</sup> In a vertical fashion they can integrate either: (i) upwards through representation of municipalities in a higher level (“regional” councils) – such representation can be direct or indirect; or (ii) top-down through deconcentration into smaller administrative areas, which might co-exist with autonomous authorities at the lower level.

<sup>60</sup> Horizontal cooperation and integration – which is critical to achieving economies of scale in areas which might otherwise be too small – can be achieved through inter-municipal agreements, although this requires strong political incentives and is seldom achieved. In India, for example, the employed fiscal capacity equalization system provides a clear disincentive for smaller municipalities to integrate into larger municipal areas.

<sup>61</sup> This then also rules out that redistributive efforts can be launched from subnational levels themselves – in Argentina and Canada, for instance, the provinces are entitled to choose formulas for redistribution in some of the financial instruments. While vertical equalization can achieve the same results from any level, such a subnational solution would create political consensus which would perhaps not exist on a nationwide scale.

### **Box 3.8: The Complex Structure of Metropolitan Governments**

Metropolitan governance is complex in many cases, and may involve several single- or multiple- purpose jurisdictions covering a whole metro area or just parts of it.<sup>62</sup> Metropolitan areas and their surrounding jurisdictions are either managed by subnational entities or have some central government involvement, given the complexity in finding purely local solutions. For example:

- New Delhi is affected by overlapping jurisdictions: power is divided among all three levels of government – center, the Union Territory of Delhi, and three municipal bodies (the Delhi Municipal Corporation, New Delhi Municipal Committee, and Delhi Cantonment).
- In Jakarta’s metropolitan area, there are three urban municipalities and three rural municipalities (districts) which belong to three provinces (Jakarta, Banten, West Java).
- Mexico City’s metropolitan area touches upon two states, a national capital district, and over 50 municipal-type local governments.
- The Sao Paulo metropolitan area (with 39 municipal governments) operates with relatively little coordination, as a supra-metropolitan entity has yet to emerge.
- The Cairo region incorporates five contiguous governorates (intermediate tier of Egyptian administration) and eight new cities. Governorates represent the central government. New cities were created to attract people from the Nile Delta to Cairo and have no formal relationship with local administration. They are overseen by the Ministry of Housing, Utilities and Urban Development (MHUUD).

Setting up a financing system which sets the right incentives for service delivery can be challenging for a metropolitan area.<sup>63</sup> Due to a high proportion of commuters, there is a breakdown of the tax-benefit principle: citizens may benefit from the public services provided by a metropolitan area but pay taxes at their residence in medium-sized towns at the outskirts. This can be the case for an automobile tax or income tax levied at residence. Cross-territorial transactions can occur more frequently in areas with many entities and jurisdictions,<sup>64</sup> and which may require higher-level administration.

Service delivery itself is challenging for several reasons—all of which limit accountability and efficiency:<sup>65</sup>

- The shifting territorial boundaries of metropolitan areas can complicate the assignment of responsibilities, as this requires both vertical and horizontal (across the different administrative areas) interventions.
- In two-tier models, economies of scale may be limited at lower levels. As metropolitan areas often emerge on top of small municipalities, there may be fragmentation across jurisdictions, at the same time that further horizontal integration is limited for political reasons.

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<sup>62</sup> Further reference in Smoke and Romeo (2013).

<sup>63</sup> For further reference refer to: Cities Alliance (2012), Kim (2013); Shah (2012); Slack (2006); Sud and Yilmaz (2013).

<sup>64</sup> Sales taxes in particular are subject to cross-territorial transactions, depending on if they are collected at origin or at destination. The corporate income tax is also worthwhile mentioning. Taxes are paid at the headquarters of an enterprise, but this might disguise the contribution of other territories when production takes place outside the metropolitan area.

<sup>65</sup> Compared to those in rural areas, metropolitan governments have higher expenditures on transport, police, and social assistance.

- Organizational arrangements can be complex: regional transport authorities; public enterprises and special-purpose districts, among others, are common and coordination among these and with entities of the SNG can be problematic.
- Metropolitan areas may not have the incentives to deliver services in all sectors. Urban entities often do deliver services with higher complexity, such as tertiary care or higher education. These services have positive externalities and spill-overs to other areas. Such incentives, however, can be mitigated with grants from the central government, although this raises the question of alignment of the different compensation mechanisms.<sup>66</sup>

As a consequence, coordination needs with other levels of government and within the metropolitan areas are significant,<sup>67</sup> and can limit accountability and efficiency. This naturally limits the ability to address the needs of the poor.

### Going forward: addressing the MDG challenge from subnational levels—three priorities

Both rural and urban SNGs face increasing challenges to influencing MDG outcomes through service delivery, which has an impact on the MDGs. Three areas of future action are critical: (i) improving public investment; (ii) fiscal equalization; and (iii) governance arrangements for accountability.

#### Public investment

Improved public investment<sup>68</sup> is a critical area as its relation to the MDGs is often direct and the infrastructure gaps in urban and rural areas are still significant. But the level of efficiency in public investment varies quite substantially across countries, even taking into account the different starting points in infrastructure quality and stock in assets, and the fact that SNGs contribute with varying degrees to public investment.<sup>69</sup> Surveys in a sample of 94 countries worldwide indicate that some OECD countries have seen decreases in the quality of infrastructure, while some countries in the developing world have taken respectable leaps forward.<sup>70</sup> This has been achieved, to various degrees, against the backdrop of either increases or cutbacks in investment spending.

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<sup>66</sup> Bahl and Bird (2013, forthcoming) refer to India, where a large federal grant for urban infrastructure development and slum upgrading is allocated to cities on a matching basis (High Powered Expert Committee 2011). The program was introduced in 2005, and while it has succeeded in focusing increased attention on urban infrastructure issues, implementation progress has been slow. South Africa makes use of a more formal municipal infrastructure grant, designed primarily to improve services in poor neighborhoods. In Brazil, ad hoc grants are made to support specific project (the authors make further reference to Rao and Bird 2011; and van Ryneveld 2007 for South Africa).

<sup>67</sup> In the social sectors, the role of the central government can be significant in cases like Dar es Salaam or Istanbul. In some of the megacities of Latin America – including Sao Paolo, Buenos Aires, and Bogota – internal coordination is required both at the metropolitan level and the municipalities below for several sectors (among others, in roads; transportation; water and sewage; waste collection; and electricity distribution).

<sup>68</sup> For a discussion on public investment and SNGs refer to: Alm (2010); Bahl and Bird (2013); Frank and Martinez-Vazquez (2013); Pagano 2011); Romeo and Smoke (2013).

<sup>69</sup> SNGs spend below 10 percent of the total, while in some countries it is up to 90 percent. This is unrelated to whether countries are unitary or federal. By and large, the share of SNGs in total capital expenditures of a country is typically twice their share in total recurrent expenditures.

<sup>70</sup> The World Economic Forum's (WEF) score for overall quality of infrastructure score is based on the responses to the Executive Opinion Survey, which polls 94 countries to top-level managers in each country from a sample of domestic and international (public and private) companies. While the data are considered fairly reliable, comparability over time is limited due to changes in the country coverage and the structure of the survey, in

Decentralized public investment is complex and might lead to inequity in spending. Project appraisal may not be sufficiently rigorous to weed out projects with questionable impact, so cost and time overruns often become apparent at later stages—when sunk costs have to be accepted. Inequities in the distribution of assets across different jurisdictions can also be significant. Public investment often implies bulky infrastructure works offering localized benefits whose distribution is influenced by political economy factors. Together, these factors can undermine equity – one of the key aspects for achieving the MDGs.

**Policy Options.** Improved public investment will require three actions:

- First, coordination across levels of government should be strengthened. Experience in OECD countries (France, Spain) has underscored that this requires reasonably strong fiscal levers. Chile, for instance, is coordinating public investment through regional investment windows, including co-financing with municipalities.
- Second, institutional and process reform should allow “poor” projects to be weeded out before they gain traction and support—while projects with high returns should be selected. Korea, for instance, has successfully addressed the “optimism bias” by requiring re-appraisal in projects with cost and time overruns.
- Third, equalization of public investment spending should be strengthened. With infrastructure gaps shifting among urban and rural areas at a quickening pace, the need for “place-based” responses to the service delivery challenge is increasing. This adequacy in resources should be provided in terms of a country’s entire expenditure needs, which include capital infrastructure, with the goal of creating a “level playing field.”

### Fiscal equalization

The incidence of both revenues and expenditures is critical for MDG outcomes. These effects can be enhanced by establishing some level of equalization to address inequities in resource distribution.<sup>71</sup> Changes in the patterns of urban-rural development imply three basic forces: (i) *citizens’ needs* change due to ongoing changes in their demographic composition, poverty profiles, and income levels; (ii) *costs of service provision* are affected; and (iii) *fiscal capacity* is affected. Fiscal equalization can address these factors.

But equalization is a complex undertaking both politically and practically. As an outcome of political negotiation, transfers are often overburdened with objectives, which may weaken desirable compensatory effects.<sup>72</sup> This can be exemplified by experience from around the world: accepting a per capita standard as a reasonable comparator, in Malawi, transfers are not establishing sufficient levels of horizontal equity (World Bank 2012). Distribution in Bolivia, in turn, is driven by hydrocarbon revenues, which bear no relation to levels of poverty in the different departments.

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particular from 2006 onwards. Importantly, the survey does not capture the various degrees of involvement of SNGs.

<sup>71</sup> For further discussion refer to: Blöchliger and Vammalle (2009); Boadway (2012); Dafflon (2012); OECD (2007).

<sup>72</sup> Some countries do organize spatially targeted programs aimed at stimulating regional development at large with a focus on the private sector, including different incentives (tax breaks, subsidies, etc.). These, however, often challenge coordination among the different interventions, including service delivery and taxation, and specific poverty and social programs.

**Policy options:** If horizontal equity is recognized as a base for addressing the MDGs, then more effort needs to be put into fiscal equalization. In fact, the increased vertical fiscal imbalances<sup>73</sup> in many countries also provide an opportunity: the share of transfers in total revenue of SNGs has increased in many cases and hence, if well implemented, its potential effect on equalization can be considerable.

Equalization can be structured vertically (across different levels), horizontally (across and among jurisdictions), or as a combination of both.<sup>74</sup> It requires defining the particular need, cost, and fiscal capacity issue to be addressed through a transfer;<sup>75</sup> defining a group of representative taxes and representative expenditures to be equalized;<sup>76</sup> and agreeing on the degree of equalization. All these decisions have both a technical and a political ingredient.

While the type and degree of equalization is, in the end, a political decision, due to the prominence of infrastructure challenges in the urban-rural dynamics, it is unlikely that full equalization for all sectors can and should be achieved. The right answer is likely to depend on the type of infrastructure and may also vary with specific circumstances, such as subnational capacity and credit availability.

- In the case of infrastructure for social services, such as health and education, the different needs may be incorporated into recurrent equalization grants because of the large presence of operation and maintenance costs.
- In the case of infrastructure that is largely fee-recoverable, such as in the case of utilities, credit facilitating policies may be the most appropriate.
- For network infrastructure that is largely non-fee-recoverable, such as no-toll roads, a conditional grant may be most appropriate.

Overall, it is clear that the starting point is not a clean slate in any country; more often than not, reforms of intergovernmental transfers are done at the margin and incrementally. This is exemplified by Colombia's current royalty reform, which achieves more equality for royalty resources in a gradual fashion. Other noteworthy efforts are currently being undertaken by Morocco, Kenya, Ethiopia, and Tajikistan, although the results are still to be seen.

### **Governance for accountability**

Accountability is critical to tackle the MDG challenge. There are two areas: (i) the way authority is constituted; and (ii) human resource management, an often forgotten but critical element for accountability and efficiency.

(i) **Authorities:** All decisions on resource distribution require institutional arrangements and the authority to exercise those decisions. These determine, to some degree, if and how costs and revenue can

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<sup>73</sup> Vertical fiscal imbalance assesses the degree of expenditures financed through own revenue.

<sup>74</sup> While overall national decisions are necessary, it would be worthwhile to analyze the extent to which fiscal equalization can be decentralized. This should be done carefully, assessing the benefits, costs, and risks of further inequality. Some countries decentralize parts of the decisions; for instance, in Argentina and Canada, provinces choose the formula for redistribution.

<sup>75</sup> This requires a distinction between two areas: (i) structural context factors should be addressed through equalization); while (ii) factors which are the result of the choice of SNGs should *not* be subject to equalization.

<sup>76</sup> The technical work and data challenge to provide meaningful indicators for cost, needs, or fiscal capacity equalization should not be underestimated; these prevent many countries from employing more useful systems.

be shared within and across jurisdictions. SNGs and their authorities can be elected or delegated.<sup>77</sup> In some cases, there are parallel and dual authorities in place, which might affect accountability. This incentive context provides the framework in which services and policies related to the MDGs need to be delivered.

**Policy options:** Institutional and governance arrangements reflect a country's political decisions, often based on its particular social, geographic, or political context. Nevertheless, as a guiding principle, a minimum level of accountability, vertically across levels and horizontally across the different territorial units, needs to be in place for MDG-relevant policies to be effective.

(ii) **Human resources.** Aside from authorities, human resources are a critical, yet often overlooked element:

- They establish institutional capacity,<sup>78</sup> a necessary condition to addressing service delivery challenges.
- They define the “fine dividing line” in responsibilities among levels of government, which is key for accountability.
- They are a significant cost driver that can impact fiscal responsibility.

Given deeply entrenched political economy factors, the risk of disjointed decision making is high. Hiring and firing decisions, along with salary policies, need to be made in a coordinated fashion.<sup>79</sup>

**Policy options:** With growing interdependencies, human resources management needs to be strengthened in an intergovernmental fashion. As these capacities are often “invisible” to citizens, which in turn rules out any demand-based reform, they need particularly strong incentives to be sustainable. These examples underscore the fact that human resources reform constitutes a challenging area that can often progress only in limited, narrowly defined service delivery areas where sufficient demand for reform exists.<sup>80</sup>

## Planning first, followed by financing

Unplanned and uncoordinated urban development can pose risks, trading the hopes of those who migrate in search of a better life for unsanitary living conditions, joblessness, and high exposure to natural disaster. Public policy makers must act now to get this rapidly paced urbanization “right” by improving access to affordable and reliable basic services such as education, housing, transport, and health care for all, and by promoting effective land use management to influence the spatial structure of cities. Isolated

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<sup>77</sup> Countries employ different models. In the vertical dimension, local governments can be represented at a higher level (bottom-up), or there can be deconcentration of a municipality into different territorial areas (top-down).

<sup>78</sup> While there is no universally accepted threshold for what constitutes an acceptable minimum level of capacity, three areas are critical as they establish a basic level of transparency: financial management, procurement, and human resources. Efforts are underway to create integrated financial management systems in many countries, including Russia (as a centralized solution), and some of the Latin American countries (Peru, and Guatemala). Some of these systems will also allow for more efficient and transparent procurement processes.

<sup>79</sup> The example of Mexico underscores some of the challenges: due to political resistance, federal teachers were not decentralized to the states, resulting in a parallel hiring process at the state level which blurred the lines of accountability. In Colombia, the early decentralization process established central pay levels, while SNGs were supposed to cover the increased cost, which was shifted back to the center through higher transfers.

<sup>80</sup> In contrast, Kenya's ambitious territorial and devolution reform has forced it to engage in a large-scale human resources reform, the results of which are still too early to be judged.

efforts are unlikely to help. Experience in managing urban growth has varied considerably across countries (see Box 3.9 for policies in the BRICS), but going forward, policy makers will need to focus on getting land management “right” and integrating the intensity of land use with the placement of infrastructure, housing, mobility, and environmental amenities.

Of course, financing rapid urban growth is challenging, as large upfront capital investments are needed to build systems for transport and water, solid waste management, and sewage removal and treatment. However, financing needs to be closely tied to how urban areas are planned and connected. Often, getting the planning in place will allow cities to leverage land and credit markets to generate finances, as well as to encourage investments by the private sector.

Integrating planning, connecting, and financing can go a long way in ensuring that urban areas enhance job opportunities, productivity, and living standards by better managing densities, and by also reaching out and improving welfare in rural areas.

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### Box 3.9: Learning from Urbanization in the BRICS

The economic motors of development are shifting from the urbanized North towards the cities of the urbanizing South, and most famously those of Brazil, Russia, India, China, and South Africa (the BRICS). The BRICS provide some inspiring examples of how to seize the opportunities that urbanization can provide. However, all went through difficult periods when they tried to resist the predictable movement of people into their cities, or steered people or enterprises to inappropriate urban locations. Several of the BRICS bear heavy burdens from past failures to accommodate urban population growth equitably and efficiently. To avoid such burdens, cities and nations need to plan proactively for urban growth, making use of both markets and planning tools, and engaging with all sectors of society, including the economically and politically weakest.

Rapid urbanization in the BRICS has generally accompanied economic growth and a shift out of agriculture, with sudden declines associated with economic and social disruption. Nevertheless, governments have been ambivalent about urbanization, even causing some of the interruptions (e.g., South Africa during Apartheid and China during the Cultural Revolution). Each country illustrates different lessons about the opportunities and risks of urbanization.

**Brazil's reluctant urbanization and the emergence of *favelas*.** Brazil's world-famous *favelas* show how failing to accommodate growing urban populations can lead to enduring social inequalities. Brazil feared that poor rural migrants would overwhelm its cities. The government failed to plan for rapid urban growth, but that did not slow its pace. Poor planning did, however, contribute to a very unequal urbanization, with large segments of the population inhabiting poorly located and ill-served informal settlements. Many inhabitants have done amazingly well under the circumstances, but these circumstances have historically been characterized by hazardous locations, enormous barriers to service delivery, bad relations with local authorities, and so on.

In recent decades, pioneering approaches have emerged: participatory budgeting in Porto Alegre, sustainable travel in Curitiba, and condominium sewerage in various cities. These and other innovations have gained international renown. The national government has introduced some of the most inclusive urban legislation, as exemplified by its ambitious City Statute. Nevertheless, the problems of the divided city, stemming from past urban policies, remain a huge challenge. In retrospect, a more inclusive and proactive approach to rural-urban migration and urban growth would have been more fair at the time and very beneficial in the long run.

**China's ardent urbanization and rapid economic growth.** China's economic transformation, which began as a rural experiment, soon became urban, involving first a string of coastal cities, then larger urban regions, then inland cities. These innovative cities soon brought vast quantities of capital from around the world together with low-wage workers from China's agricultural regions. The central government progressively loosened controls on private investment within the city and on temporary rural migration into the cities. Economic powerhouses arose incrementally from locally driven but centrally sanctioned urban experimentation. City governments were given increasing powers and put under enormous pressure to raise economic production. A dominant model emerged of entrepreneurial city bureaucrats taking lead roles in land conversions. They oversaw the transformation of low-value urban or rural land into serviced plots whose long-term leases were sold at near-market prices to real-estate developers, or at lower prices to investors promising industrial or commercial establishments.

China's stunning economic success highlights the importance of achieving moderately efficient urbanization for economic growth, but it is based on policies other countries would struggle to replicate, and has brought unenviable environmental costs and social inequalities. China has recently tried to reduce these detractions while maintaining rapid economic growth, but it has been difficult to challenge the existing model, whose

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success is based on closely aligning local authorities' official and unofficial interests with market pressures, even when that causes environmental damage or amplifies inequalities. Urban experimentation could still hold the key to progress on social and environmental agendas, but local alliances of entrepreneurial bureaucrats and developers are unlikely to drive these agendas.

**Russia: cities in the wrong places.** Russia's urbanization history shows how long-term economic growth requires people and economic enterprises to move to productive urban locations — not just to anywhere in any city. This is a difficult process to direct unless markets are allowed to play a larger role than permitted by the Soviet authorities.

From an economic perspective, the Soviet system located many urban activities and populations in the wrong places. Non-market decision making left many cities exposed at the end of the Soviet era. The need for spatial restructuring brought heavy social and economic costs, adding to the traumas that accompanied the dismantling of the Soviet central planning system. Populations shifted towards newly vibrant cities and service centers in the south and west, and away from industrial cities with few amenities in the far north and east. This may be the right response from an economic standpoint, but has involved considerable dislocation. Cities that produced goods for the military-industrial complex, or consumer goods protected from competition, have suffered enormously, even as those with natural resource bases or other strengths in the market economy have thrived.

**South Africa's apartheid urban controls and its fragmented cities.** South Africa's Apartheid system was an extreme lesson in the dangers of exclusionary urban policies, particularly when combined with overt discrimination against particular social groups. Since Apartheid ended, urbanization has rebounded, but the inherited social and economic divisions have proven to be intractable. The low density, fragmented form of South African cities has also had harmful social, economic, and environmental consequences, some of which are only beginning to be addressed. It has imposed additional barriers to employment for the poorest communities, added to the cost of bulk infrastructure provision and public transport, and fostered carbon-emitting private transport.

The creation of constitutional rights for the poor has helped to promote their cause, but has not always been backed by political will and sufficient government resources to meet people's basic needs for electricity, water, and sanitation. Equally important are city-level leadership and investment plans that integrate fragmented cities more effectively, boost jobs and livelihoods, and work with poorer communities to improve essential services.

**India: ambivalence to urbanization offers an uncertain future.** India is less urban than the other BRICS, and its ambivalent attitude to urbanization could impede economic progress, at least for the low-income groups who find it increasingly difficult to secure a place in India's cities. The size of India's still-growing population that has to find sustenance in rural settings is daunting. India's current challenges illustrate the importance of taking the rural implications into account when designing urban policies.

This is a particularly critical time for India's urban policies as they will help to determine whether economic growth is maintained, who will benefit, and what the environmental consequences will be. The Indian government has initiated several important programs intended to support equitable and efficient urban development, including the Jawaharlal Nehru National Urban Renewal Mission (JNNURM) and Rajiv Awas Yojana (RAY). India has also pioneered civil society and grassroots efforts to improve conditions for deprived urban dwellers, including the partnership between the Society for the Promotion of Area Resource Centres (SPARC), Mahila Milan, and the Indian National Slum Dwellers Association. To meet its urbanization challenge, India must not only address existing urban poverty, but also create cities that can accommodate rapid urbanization and give even the poorest rural dwellers a fairer share of the benefits of economic growth.

*Source:* Contributed by IIED and UNFPA.

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## Annex 3.1: International Financial Institutions and Urbanization

International Financial Institutions (IFIs) have long been engaged in supporting the urbanization process through different lending and non-lending mechanisms. These include a range of responses from financial support to improve housing conditions for slum-dwellers to strengthening transport services to reduce congestion costs to integrated knowledge products that help countries plan better for anticipated migration from rural areas to its cities as well as address issues of congestion from natural growth of urban areas.

### African Development Bank

The African Development Bank (AfDB) Group recognizes that the continent's cities and towns can be a major driving force for economic development. In 1992, its Board approved an Urban Development Policy to: provide guidance for AfDB Group operations in the urban sector; build a foundation for dialogue with counterparts; and promote cooperation with other development partners. The policy targeted regional member countries' (RMC) capacity to plan and implement investment programs, promote private initiatives, support decentralization, and upgrade human resources. Also important was improving the living conditions of the urban poor. The AfDB has supported urban development over the years through projects in public utilities, industry, transport, education, health, and other social interventions. Between 1967 and 2007, roughly 15-20 percent of the cumulative financing provided by the AfDB Group benefited urban dwellers and enterprises either directly or indirectly.

In 2011, the AfDB developed its urban strategy (*"Transforming Africa's Cities and Towns into Engines of Economic Growth and Social Development"*), which was aimed at enhancing the effectiveness of its interventions in urban development in Africa. The main objective of the strategy is to boost the viability and competitiveness of African cities to help them enhance their role as engines of growth and economic development. The strategy focuses on three main pillars in alignment with the AfDB's core areas of interventions: (i) infrastructure development; (ii) urban governance; and (iii) private sector development. The urban strategy is based on the AfDB's medium-term plan for 2008-2012 and the 2009 mid-term review of the African Development Fund (ADF), the concessional financing window of the AfDB. The urban strategy aims at helping RMCs make progress towards the achievement of MDGs and also helps in mainstreaming the key cross-cutting issues concerning all urban operations, namely knowledge generation and management, regional integration, environment, climate change, gender, and empowerment of vulnerable populations. An illustration of the purpose of the strategy, outcomes and targeted results by 2015 is summarized in Table A3.1.

**Table A3.1: AfDB's urban development strategy: purpose, outcomes and targeted results by 2015**

Purpose of the Strategy	Partners Institutions	Medium-Term Country Outcomes	Beneficiaries	Performance Indicators	Indicative Targets
Improve access to infrastructure services, governance and private sector participation in African cities through enhanced effectiveness of AfDB Operations in RMCs urban sector.	World Bank, IFC, UN-HABITAT, Cities Alliance Bilateral agencies such as AFD, Sida African organizations such the Municipal Development Partnerships and Shelter-Afrique. Islamic Development Bank UCLGA	1. Improved access to urban infrastructure  2. Conditions in slums improved  3. Public-Private Partnerships enhance service delivery  4. Local government finances are strengthened	Urban population Local and central governments RMCs	1.1 Urban population with access to safe drinking water (WHO-UNICEF) 1.2 Urban population with access to adequate sanitation (WHO-UNICEF) 1.3 Percentage of population in urban areas provided with access to all-season roads. 1.4 Percentage of population with access to environmentally friendly mass transit systems 1.5 Number of urban people with access to electricity 1.6 Number of people with access to broadband connectivity 1.7 CO2 emissions per US\$ of GDP.  2.1 Number of Major slum upgrading schemes/urban poverty programs in progress (Cities Alliance, UN-HABITAT) 2.2 Number of RMC reform of legal & regulatory frameworks for pro-poor housing delivery (AfDB assessment) 2.3 Increase in the percentage of women and youth employed in urban infrastructure works and SMEs 3. RMCs with PPP in urban service delivery (PPI database) 4.1 Increase in the percent of local government's contribution to the total expenditure (UCLG, IMF, AfDB, WB) 4.2 Number of Transparent systems for transfers to municipalities (AfDB & WB assessment) 4.3 Local government revenues (UCLG, IMF, AfDB, WB)	1.1 Progress consistent with MDG Target 10 (93% in 2015 ; baseline 85% in 2006). 1.2. Progress consistent with MDG Target 10 (76% in 2015; baseline 53% in 2006) 1.3 10% increase by 2015  1.4 10% increase by 2015  1.5 10% increase by 2015 1.6 20% increase by 2015  1.7 CO2 emissions decline to 1.4 kg per 2000 US\$ of GDP. (Baseline 1.67 kg per 2000 US\$ of GDP in 2004) 2.1 Programs/ schemes initiated in 4 RMCs  2.2 Reforms in 4 RMCs by 2015  2.3 10% increase by 2015  3. The number increased to 18 in 2015 (from 13 in 2008)  4.1 20% increase by 2015  4.2 Transfer system reformed in 4 RMCs  4.3 LG revenues as % of GDP increased in AfDB's projects

Implementation of the AfDB's urban strategy will exploit the AfDB's existing financing instruments using the central governments' channel, which include: (i) loans and guarantees, mainly to middle-income countries (MICs), and private sector loans to MICs and low-income countries (LICs); (ii) loans and/or grants from the ADF window to LICs and fragile states; and (iii) trust funds and other facilities. For sub-sovereign financing in the case of credit-worthy municipalities, the AfDB will invest in knowledge generation and lessons from other institutions concerned with this type of financing.

In recent years, the AfDB has supported up to 70 urban related projects and initiatives, such as: improving *Zanzibar's Water Supply and Sanitation services* worth (UA 28m); the *Dakar-Diamniadio Highway Project* (UA 45m); the *Nairobi - Thika Highway Improvement Project* (UA 121m); and the *Conakry Electrical Networks Rehabilitation and Extension Project* (UA 12m). Since 2000, the AfDB's financial commitment for urban development interventions has amounted to UA 2.26 billion (US\$3.5 billion). The AfDB has also invested in various other interventions that have played a role in improving the socio-economic levels of both the urban and rural populations, such as inputs towards increased access to energy and transport facilities and in promoting regional integration. Table A3.2 illustrates some of the key results delivered in these areas in 2010-2012.

**Table A3.2: AfDB's deliverables in 2010-2012 in energy, transport and regional integration**

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Indicator	
<b>Energy</b>	
Length of transmission and distribution lines rehabilitated or installed (km)	13,129
Distribution substations and transformers constructed or rehabilitated (number)	Expected
Power capacity installed (MW)	780
Staff trained/recruited in the maintenance of energy facilities (number)	1,963
People with a new electricity connection (number)	203,602
Population benefiting from new electricity connections (people)	6,498,853
<b>Transport</b>	
Roads constructed, rehabilitated or maintained (km)	15,695
Feeder roads constructed or rehabilitated (km)	7,994
Staff trained/recruited for road maintenance (number)	13,950
People educated in road safety and HIV transmission (people)	810,000
People with improved access to transport (people)	40,326,880
<b>Regional Integration</b>	
Cross-border roads constructed or rehabilitated (km)	471
Cross-border transmission lines constructed or rehabilitated (km)	597

Source: AfDB 2013.

The AfDB has also undertaken economic sector work, such as a *Study on the Expansion of Monrovia's Water Supply and Sanitation System* (UA 1.5m). Moreover, following its 2008 Annual Meetings in Maputo where the High-level Symposium addressed issues on *Urbanization, Inequality and Poverty in*

*Africa*, in 2009 it embarked on a research program in partnership with SIDA aimed to yield knowledge products to assist AfDB staff and RMCs in addressing urban development issues. A key product of this partnership is a book titled *Fostering Shared Growth: Urbanization, Inequality and Poverty in Africa*, due for publication in 2013.

An exemplary project illustrating the impact of AfDB's projects on the lives of the urban poor is the Poverty Reduction Project in Ghana (Box A3.1).

### **Box A3.1: Tackling Urban Poverty in Ghana**

As urbanization has proliferated in Ghana, particularly in the Central and Northern regions, the level of urban poverty has also been on the increase. An estimated 2 million urban dwellers in Ghana are classified as poor. In Accra alone, 45 percent of the population has lived in the poorest neighborhoods with lack of water, sanitation, and educational facilities since the 1990s. As a pilot country, Ghana benefited from the AfDB urban poverty reduction project worth about US\$40.25 million.

The objectives of this project were to: (i) develop urban settlements through participatory management, job creation and strengthened public-private partnerships and local governance and management capacity; (ii) improve living conditions in urban and peri-urban zones by increasing access to basic quality services and socioeconomic infrastructure; and (iii) facilitate access to income generating activities through capacity building and a strengthened urban small-scale enterprise sector.

The project covered 12 metropolitan, municipal, and secondary towns of 4.45 million people. The expected benefits included improvement in the livelihoods of the urban poor through better access to good socio-economic infrastructure, creation of 6,000 jobs for unemployed youth, and skills development training for at least 4,000 women. The project was expected to generate 350 and 50 urban and peri-urban socio-economic and environmental sub-projects, respectively.

*Source: AfDB 2011.*

## **Asian Development Bank**

The Asian Development Bank (ADB) has sought to facilitate the structural transformation for successful urbanization by providing various instruments, financial and knowledge-based, to its client countries. Of project financing identified for rural and urban development projects, approximately US\$3.3 billion was allocated for urban development and US\$2.3 for rural development in 2012. In rural areas, the transport and ICT sectors received the most, at 45 percent in 2012; agriculture was well behind, with 25 percent of the total allocation for rural development in 2012. In urban areas, the largest sector is also the largest sector, receiving 35 percent of the total allocation for urban projects; energy received 24 percent, and water supply and other municipal services received 17 percent in 2012. Note that the ADB has slowly increased its allocation to support urban development from around 50 percent in 2008 to close to 60 percent of a growing amount of total resources available for both areas of development.

## **East Asia – People's Republic of China (PRC) and Mongolia (MON)**

Support for "urban-rural dynamics" in the People's Republic of China (PRC) and Mongolia (MON) is broadly in line with ADB's support for inclusive growth. ADB operations help address regional and urban-rural disparities, improve rural livelihood, and facilitate urbanization with job creation for migrant workers.

In the **PRC**, more than 90 percent of ADB's operations are focused on the lesser-developed central, western, and northeastern regions to promote regionally balanced and integrated urban-rural development. Transport operations have facilitated movement of people for better access to job opportunities and public services, particularly among migrant workers. Urban operations have supported integrated urban-rural infrastructure development and improvement of urban services, including provision of employment services and technical and vocational education and training. Natural resources and agriculture operations have supported biomass energy and water and natural resources protection, which help generate income and expand livelihood improvement opportunities.

The PRC government is accelerating its support to organize the development of the country's small- and medium-sized cities. The country's macro urban strategy aims at rationalizing the unbalanced urban structure at all levels of the urban hierarchy, which currently provides a weak base for supporting a sustainable and inclusive development. Operational activities including urban and social sectors in the last five years focus mainly in the poor northeastern and western central inland regions of the PRC. The approved loan amounts for urban development ranged from around US\$485 million in 2008 to US\$350 million in 2012. These projects aim to enhance the development potential of small- and medium-sized cities, thereby directly and indirectly providing support to reduce regional imbalances and income disparities between urban and rural areas. Especially for urban-rural integration, Chongqing Municipality provides a good example. ADB has been a close partner of the Chongqing Municipality, the first provincial-level demonstration area for piloting urban-rural reforms in the PRC. In 2010, the first US\$100 million Chongqing Urban-Rural Infrastructure Development Demonstration Project was approved to finance key infrastructures of urban-rural roads and small scale potable water supply plants in eight poor districts and counties of Chongqing. In 2013, ADB and the PRC government are working on a proposed US\$150 million loan project for the second phase, which will further demonstrate more balanced and inclusive urban-rural development in Chongqing.

The total population of **Mongolia** was 2.8 million in 2011, including 1.3 million inhabitants living in Ulaanbaatar City. Forty percent of Ulaanbaatar's population lives in the city core while 60 percent (approximately 800,000 people or about 30 percent of the national population) live in peri-urban (ger) areas. During the last five years, the population growth of the whole country was around 220,000 inhabitants. Almost all the population growth, about 210,000 persons, went to Ulaanbaatar City. The countryside population decreased dramatically while the aimags' capitals and other small cities' populations remained almost stable. The population growth of Ulaanbaatar City mainly happens in the ger areas of the City and represents 75 percent of the total national population increase. Despite their size, ger areas have been considered merely temporary settlements and therefore have never been formally integrated in the city development process and infrastructure programming. Thus, the continuing ger area densification and sprawl is putting tremendous pressure on the urban environment. The huge gap between services in the formal and ger areas remains one of the most difficult challenges for the government, especially as projection indicates that ger growth will be around 350,000 more during the next 10 years.

Approved loans in Mongolia during the last five years amounted to about US\$78.2 million. This includes improving water and other municipal infrastructure and services in South-East Gobi desert small towns (US\$15 million ADF approved in 2010) and the improvement of urban transport in Ulaanbaatar city (US\$29.7 million OCR and US\$30.2 million ADF approved in 2012). In 2011, a Public-Private Transportation Act was approved, under processing, to prepare a multiannual financial framework for improving Ulaanbaatar City urban services and ger areas development.

### Central and West Asia – Multisector Sector Assessment for Kazakhstan and Uzbekistan

In addition to financial support, the ADB also provides analytical services to facilitate decision making by policy makers faced with urban and rural development challenges. For example, in Kazakhstan, the Country Partnership Strategy (2012-2016) includes a detailed sector assessment of urban transport and water and sanitation (<http://www.adb.org/sites/default/files/cps-kaz-2012-2016-ssa-03.pdf>). In Uzbekistan, the Country Partnership Strategy (2012-2016) assessed issues surrounding water supply and sanitation, waste management, urban transport, and other municipal services (<http://www.adb.org/sites/default/files/cps-uzb-2012-2016-ssa-04.pdf>).

The urban regional technical assistance projects fostered the work of the Urban Community of Practice and, in particular, the Cities Development Initiative for Asia (CDIA), an International Partnership Program assisting medium-sized Asian cities to bridge the gap between their development plans and implementation of their infrastructure investments. CDIA uses a demand-driven approach to support the identification and development of urban infrastructure investment projects in the framework of existing city development plans that emphasize one or more of the following impact areas: (i) urban environmental improvement; (ii) urban poverty reduction and gender; (iii) climate change mitigation or adaptation; and (iv) improved governance.

To facilitate these initiatives at city level, CDIA provides a range of international and domestic expertise and advice to cities to move from strategic master plans to concrete policies and infrastructure projects ready to present to financiers and project developers. Core city-level CDIA activities comprise a range of measures typically including one or more of the following elements:

1. **Infrastructure investment programming and prioritization:** Advisory support for undertaking infrastructure investment programming and prioritization.
2. **Pre-feasibility studies (PFS):** Consultancy support to undertake preparation of PFS on high priority infrastructure investment projects and demonstrating integration within a city's overall development process.
3. **Linking cities to finance:** Identification of financial sources for selected investments from domestic and international finance markets as well as opportunities for PPPs.
4. **City-level capacity development:** Local institutional capacity strengthening through on-the-job training related to infrastructure investment planning and programming and project management.

As of December 2012, CDIA had approved applications from four cities in 13 countries with a number of others under consideration. These interventions are estimated to lead to about US\$6.5 billion in strategic urban infrastructure investments. In the current portfolio, urban transport is the largest CDIA sector, followed by flood and drainage management, urban renewal and wastewater management. While ADB and KfW are the primary downstream financiers, increasing emphasis is being placed on assisting cities to bring in additional financing through PPPs. While the impact emphasis focuses on environmental

improvement, poverty reduction, and governance aspects, CDIA's work has invariably contributed to a wider set of cross-cutting impacts. Especially through capacity strengthening, CDIA has contributed to improved governance with city partner agencies. See also **Green Cities**, November 2012 (<http://www.adb.org/publications/green-cities>).

## **European Bank for Reconstruction and Development**

The activities of the European Bank for Reconstruction and Development (EBRD) that address the issues related to urbanization differ from those implemented by other multilateral development banks. The EBRD has a specific mandate that identifies supporting its countries of operations in their transition to market economies as the main goal. Through provision of a variety of products (both investment and technical co-operation) to private and public sector clients representing a range of different sectors, the EBRD therefore has a specific role to indirectly address the urbanization issue. This role involves improving the business environment and removing infrastructure bottlenecks, both of which are crucial in facilitating the urbanization process in EBRD's 34 countries of operation. Examples of such activity of the EBRD in the private sector include specifically targeting enterprises in rural underserved areas through an MSME finance loan or supporting the involvement of farmers by extending backward linkages in agribusiness.

The EBRD also plays an active role in helping put adequate infrastructure in place to facilitate the changing urban-rural dynamics and to minimize the negative impact of urbanization on cities. The EBRD's activities in the water and wastewater sector aim at achieving an enhanced and sustainable provision of services to urban populations. These operations are based on sustainable cost-recovery tariff structures, the development of robust regulatory approaches with a focus on the modernization of infrastructure, the promotion of appropriate environmental, social, health, and safety improvements that result in high-quality service delivery, and management efficiency. Since its inception, EBRD has rapidly expanded its activities in the water and wastewater sector throughout its countries of operations. To date, EBRD has financed over 130 water and wastewater projects, for a total of EUR 2 billion.

Improvement in urban transport, in which EBRD has been actively involved, is another essential component of facilitating urbanization processes. Urban transport has a unique ability to provide high-quality alternatives to private car use, and as such acts as a viable antidote to urban congestion and pollution, the latter two being negative consequences of urbanization. Urban transport provides value-added to the urban environment and increases the general quality of life for the urban population by improving air quality, reducing delays due to congestion, and contributing to carbon reductions. The EBRD has financed over 60 urban projects in different countries of operation, for a total of EUR 1.4 billion. The EBRD addresses complex issues related to a variety of existing bottlenecks in the urban transport sector by implementing an integrated approach that consists of investments, technical assistance aimed at improving management capabilities, and policy dialogue with local and national authorities to strengthen the regulatory and institutional framework.

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**Box A3.2: EBRD's Integrated Approach to Transition Challenges in Almaty's Urban Transport Sector**

Fuelled by a number of factors, including economic, social, and structural changes in Kazakhstan over the last decade, the population of Almaty, the country's biggest city, has been steadily growing. This is in large part a result of internal migration of the workforce from rural areas. The population of Almaty is expected to reach 1.6 million, compared to 1.1 million in 2000. In the urban transport sector, this has been punctuated by a steady rise in private car usage, which subsequently led to a change in Almaty's transport pattern. The car fleet in circulation increased from 218,000 in 2003 to 560,000 in 2011. Greater reliance on cars for urban transportation mobility has increased road congestion and general urban livability in Almaty. Air quality in Almaty is severely affected by pollution from traffic, and in particular, by emissions resulting from the use of low quality fuel, a badly maintained and outdated private car fleet, and ever increasing congestion compounded by insufficient road management. In general, there has been an underinvestment in public transport solutions and traffic and parking management; institutional weaknesses and deficiencies in regulatory frameworks have also been identified as issues negatively impacting the effective development of urban transport.

To address these complex challenges, EBRD is pursuing an integrated approach to the urban transport sector in Almaty involving investments in target projects coupled with extensive technical cooperation and policy dialogue activities. Together, these activities aim at setting new standards for service quality in public transport, establishing a solid foundation for the introduction of a new regulatory framework in the sector, and integrating private operators into one client-oriented system with significantly improved service standards. To address the growing traffic problems and increasing dependence on private car usage, the EBRD's investments aim at increasing the capacity and standards of public transport services as an alternative to car usage and providing an overall balanced approach to urban mobility with viable travel choices for users. The investment projects include major investments in a modernized clean urban bus (CNG) and a trolleybus fleet to provide a sector benchmark to the private sector. Finally, an integrated e-ticketing system operated under a build-operate-transfer concession will be implemented across all public transport services to allow for network effect benefits (i.e., increased ridership due to free transport modal transfers) to accrue to the operators.

The EBRD's policy dialogue will focus on institutional development of the sector in Almaty and will include, among other activities: (i) design and creation of a robust regulatory approach through creation of new urban transport authority; (ii) improvements of the contractual agreements to enable financing investments by private operators; and (iii) introduction of an integrated electronic fare collection system. In parallel, the EBRD's efforts will be complemented by World Bank and UNDP assistance aimed to support the city in preparation of activities designed to improve the functioning of and benefits produced by the sector (development of computer-based traffic model, new comprehensive route scheme, and carbon emission reduction assessment methodologies for the sector). It is expected that the EBRD's activities in the urban transport in Almaty, in close collaboration with other IFIs, will contribute to creating efficient and effective market mechanisms in this sector and help mitigate negative consequences of urbanization in Almaty.

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## **Inter-American Development Bank**

The Inter-American Development Bank (IDB) established an Emerging and Sustainable Cities Initiative (ESCI) in 2011, since urbanization is taking place at a very fast pace in Latin America and the Caribbean (LAC). Already the second most urbanized region in the world, LAC went from 62 percent urbanization in 1980 to 81 percent in 2011. If this trend continues, in 20 years most of the region's population will be

living in cities (90 percent or more). Although large cities are more prevalent in LAC than in developing countries in other regions, these megacities are no longer those with the highest rates of growth and the region's urban population increasingly consists of residents of intermediate rather than large-size cities (Lora 2010). This pace of urbanization is creating daunting challenges for intermediate and emerging cities in the region.<sup>81</sup>

These emerging cities are still characterized by unacceptably high proportions of the population living in poverty, with limited governance and an enduring scarcity of resources. The challenges are multiplied when considering the efforts of cities to cope and adapt with the adverse effects of climate change. Events such as flooding and storm surge increasingly impact cities in the region, generating significant economic losses. Political decentralization has advanced substantially in the region over the last two decades. Local governments have assumed greater responsibilities for the provision of social services. However, fiscal decentralization has not kept the same pace and most municipalities are not fiscally independent and do not manage their fiscal affairs well. They have very limited fiscal space to accommodate necessary investments in sustainability, and in most of the cases are not credit-worthy partners to the private sector (PPPs transactions). Their capacities to improve quality of life of their citizens are limited.

### **Emerging and Sustainable Cities Initiative (ESCI)**

In 2011, the IDB launched the Emerging and Sustainable Cities Platform. The first phase was the pilot test to develop ESCI's methodology and its application in five cities: Trujillo in Peru; Port-of-Spain in Trinidad and Tobago; Santa Ana in El Salvador; Montevideo in Uruguay; and Goiania in Brazil.

On February 2012, the Bank's Board of Directors approved the second phase, the development of the ESCI, which includes scaling up of the program to a total of 26 cities in the region between 2012 and 2015. The general purpose of the Initiative is to improve the sustainability and quality of life in emerging cities in Latin America and the Caribbean in terms of three comprehensive dimensions [pillars]: (i) environmental sustainability and climate change; (ii) sustainable urban development; and (iii) fiscal sustainability and governance.

The ESCI employs a multidisciplinary approach to addressing the challenges facing the urban areas of LAC, by integrating environmental sustainability, comprehensive urban development, fiscal sustainability, and good governance. The Initiative provides a set of tools for intermediate cities to be able to: (i) identify key bottlenecks that they may face in their path towards sustainability; (ii) weigh and prioritize the identified problems to guide investment decisions in the sectors that may generate more positive impacts; (iii) find specific adequate solutions according to their cost-benefit that would pave the road towards increasing sustainability ("prioritized interventions"); and (iv) follow up on progress and advances in closing gaps and reaching goals.

The Initiative works in three key dimensions:

- The *environmental and climate change dimension* is concerned with environmental management and local pollution control issues (including air and water contamination, solid waste

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<sup>81</sup> Emerging cities are defined as cities between 100,000 and 2,500,000 inhabitants growing – economically and demographically – above the national average. At present, Latin America and the Caribbean has more than 140 emerging cities, with a total population of about 70 million inhabitants.

management, and disaster prevention), climate change mitigation (through energy efficiency and other measures), and climate vulnerability reduction and adaptation measures.

- The *urban development dimension* refers to the effects of the city's design and footprint (or its ability to control its growth through effective planning and land use control), social inequality and uneven distribution of urban services, efficiency of its urban transportation network, economic competitiveness, and the level of public safety.
- The *fiscal sustainability dimension* is related to the ability of local governments to prioritize and finance needed investments, fund and maintain their urban and social services, control adequately their expenditures and debt, and make decisions in a transparent manner.

### **ESCI's Methodology**

Deployment of the Initiative in cities consists of two distinct stages:

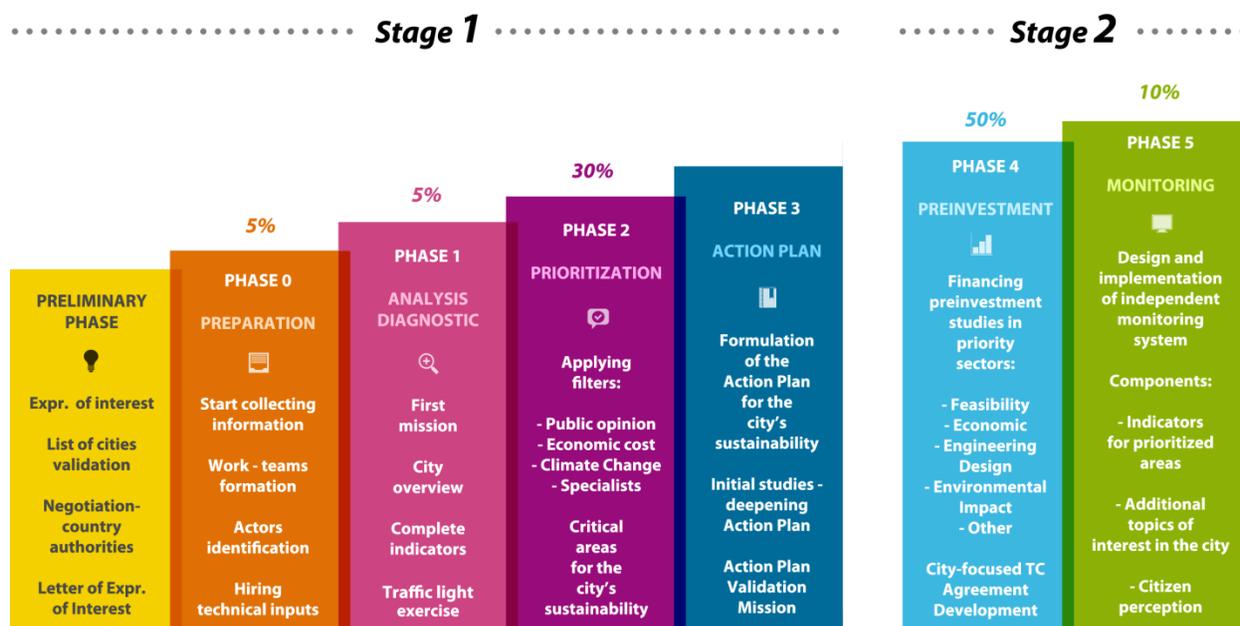
#### ***Stage 1 – Application of the ESCI Methodology (phases 0 to 3), Development of the Action Plan:***

ESCI's methodology consists of: data collection, analysis and diagnosis, prioritization via the application of different filters (environmental, economic, public opinion, expert opinion), and formulation of an Action Plan where priority is given to activities necessary to improve existing conditions and to determine the resources and times required to complete them. Besides this, the IDB ensures support for generation of expertise and diffusion of innovative experiences among the cities' governments.

The IDB together with McKinsey Consulting Firm developed a rapid assessment diagnostic tool around the three abovementioned pillars. This tool involves the analysis of 150 indicators, and provides, in a period of six months, a comprehensive diagnostic of the situation of a particular city. The diagnostic is followed by a prioritization process that includes extensive consultation with civil society, academia, and local government as well as a public survey among citizens. This exercise leads to the development of an Action Plan, including key strategic interventions.

#### ***Stage 2 – Pre-Investment and Monitoring Process (phases 4 and 5), Action Plan Execution:***

Once developed and agreed among local stakeholders, the Action Plan moves into the execution phase, where the Initiative assists in the design and development of the pre-investment components of at least one priority intervention as well as in the mobilization of financing from different sources (i.e., public sector budget, private sector capital via PPPs, commercial bank financing, MLAs, etc.). The execution phase also includes the implementation of the monitoring system via the participation of local non-governmental organizations (NGOs), the private sector, and academia.



### Financing of the ESCI Program

The Bank has established a Special Fund (US\$25 million) to support provision of non-reimbursable technical assistance to cities adopting the ESCI methodology. The funding covers the development of all the phases in the ESCI Methodology. To be able to expand and replicate the ESCI program in the region, the Initiative considers additional funding from third interested parties. This could be represented by government resources, private foundations, academic institutions, and international donors. Most of the donor resources come in the form of grant contributions to an ESCI multi-donor trust fund. However, some of the contributions are also given in kind (staff time, consulting work, etc.) by some institutions interested in the program. Cities funded from third parties are considered part of the Additional Program. In these cases, ESCI also contributes to the partial funding for methodology implementation.

The Initiative will include all member countries in the region and will be open to any municipality, state or provincial governments, or groups of municipalities. However, the initial priority will be to focus on medium-size cities, the 70 emerging local economies of the region, where the impact of the actions has the potential to be greater and more immediate. The Initiative is aimed at mobilizing and coordinating the technical capacity of all the areas of the Bank in supporting the cities in closing the gaps identified and prioritized in the process.

### ESCI Implementation (2011 - 2015) and Preliminary Results

#### 2011 - Pilot phase

Five cities were selected to test the methodology and set the Initiative in motion. The following preliminary selection criteria were established: (i) city population between 100,000 to 2,000,000 people depending on the overall country population; (ii) availability of information that will allow for the construction of an indicators system to be proposed as part of the methodology; (iii) an existing planning framework (planning process, urban and environmental plans, etc.) that will provide the initial institutional support required for the application of the proposed methodology and the development of the Action Plan; and (iv) strong leadership from the city Mayor's office and/or the specialized

urban/environmental sector that would guarantee full participation and support during the execution of the consultancy, as well as medium- and long-term commitment to sustainability objectives. The five selected cities were: Goiania (Brazil), Trujillo (Peru), Santa Ana (El Salvador), Port of Spain (Trinidad and Tobago), and Montevideo (Uruguay).

## **2012**

The five cities included in the pilot phase have already completed their action plans and work is advancing towards the execution of the plan and implementation of the monitoring system. Some of the prioritized interventions in those cities were:

- Integral Urban Upgrade Renewal in East Port of Spain, Trinidad and Tobago
- Urban Transport (mobility) in Trujillo, Peru
- Monitoring Center for traffic, security and natural disaster prevention (connectivity) in Goiania, Brazil
- Integral Urban Upgrade in Casa Valle, Montevideo, Uruguay
- Increase water access and improve water resource management in Santa Ana, El Salvador.

Eleven more cities were added during 2012. Five of the cities were added via the Regular program: Mar de Plata, Argentina, Cochabamba, Bolivia, Managua, Nicaragua, Montego Bay, Jamaica and Barranquilla in Colombia. The remaining six cities were added via the Additional Program. La Paz, BCS, in Mexico was added via the Special Program with funding from two private sector foundations (ICF and FEMSA) and has already completed its Action Plan. Manizales, Pereira and Bucaramanga were added via a strategic partnership signed with Findeter (National Development Bank assisting municipalities) in Colombia. Two more cities, Salta in Argentina and Valdivia in Chile, have initiated the application of the ESCI methodology with their own funding. With the exemption of La Paz, BCS, all of the 2012 cities are currently completing their Action Plans.

## **2013**

Five cities from the Regular Program have already been selected and work is expected to start in the first semester of this year (i.e., Asuncion in Paraguay, Cuenca in Ecuador, Cap Haitien in Haiti, and cities to be determined in Guatemala and Mexico).

ESCI will initiate this year the pilot plan with the second strategic alliance with a local development bank to launch a national program. ESCI together with *Caixa Economica Federal* in Brazil will initiate work in two additional Brazilian cities in the second quarter of this year. Negotiations are also currently taking place with the Government of Argentina to expand ESCI at the national level and include additional cities.

## **Scale Up**

The objective is to include approximately 50 emerging cities located in different countries of the region by the end of 2015. ESCI will continue exploring the options of deploying the program via strategic partnerships with local development banks in the region during the next three years.

## The World Bank

The World Bank has maintained a large presence in the area of rural and urban development. However, it has particularly scaled up its knowledge-based services regarding urbanization, in particular through the Urbanization Knowledge Platform, which focuses on collaboratively building the evidence-base for sustainable urban development.

Effectively managing the rapid change associated with urbanization is no easy task. And the risks are high, because many of the decisions that city leaders make today may forever lock cities onto an unsustainable path of development. To help cities avoid this fate and harness urbanization for sustainable and inclusive growth, it is not enough for institutions like the World Bank to be only a producer of knowledge—they must also be customizers, connectors, and catalysts for knowledge. This means translating global evidence and best practices into local solutions. It means connecting cities with one another to exchange best practices and learn from one another. And it means catalyzing new research by making data openly available to the public, so that others can validate conclusions, build from the findings, and contribute to development solutions.

To operationalize this approach, the World Bank launched a global knowledge partnership around the transformational topic of urbanization in 2011. The Urbanization Knowledge Platform (UKP) seeks to *convene and connect* city leaders, national policy makers, academia, the private and third sector, and development agencies from around the world to *co-create and customize* new insights on the most pressing challenges and opportunities faced by cities. Its mission is to put the world's best knowledge and data in the hands of policy makers so that they can better harness urban growth for sustainable and inclusive development.

The UKP began its activities by convening and co-hosting over 20 high-level policy consultations and knowledge exchanges in partnership with local think tanks, regional teams, and policy makers in 14 countries on five continents. Collectively, these events consulted over 800 city leaders and 4,000 other stakeholders to facilitate extensive south-to-south knowledge exchange, convene regional stakeholders around common challenges, and lay the groundwork for future partnerships to jointly fill knowledge gaps. For instance, the platform facilitated regional knowledge exchanges among mayors for shared learning, such as by forming a community of city leaders from eight countries in South Asia for unprecedented city-to-city learning that sidestepped inactive cooperation at national levels. And it nurtured global PPPs of over 60 organizations to help harness and tailor the promise of “smart city” and “smart climate” innovations to the needs of low-income countries.

Crucially, these global exchanges also led to the identification of the most pressing challenges and opportunities faced by cities. The city leaders consulted through the platform asked the World Bank: What must be done to create jobs? What must be done to improve living conditions in slums and hazard-prone areas and to bridge the social divide? What must be done to expand the coverage and quality of basic services?

So what has been learned to date? First, there are no straightforward answers to these questions, and the evidence base on many of these issues is filled with critical knowledge gaps. But the UKP's discussions with hundreds of city leaders from around the world also taught that, while all cities are unique, the

challenges they face are remarkably similar, even across stages of development—with shared issues ranging climate change to social inclusion. This means that “*know how*” and *solutions are transferable*; that the lessons learned from one city can—and should—inform the choices of cities on the other side of the planet. In other words, while it is known that there is no single blueprint for success, it is the case that some countries and cities have been more successful than others. There is a need, therefore, for the aspiring cities of today to learn what worked and what didn’t from those that have gone before and to collaborate on common solutions to shared problems informed by the evidence. Such shared learning and collaboration has been obstructed by a lack of facilitating global public goods (forums, knowledge platforms, open data, etc.) The World Bank through the UKP aims to help fill this gap and to provide the role of knowledge broker.

Second, most cities face not just a single bottleneck to sustainable development, but often a wide range of challenges that require *integrated solutions and tight policy coordination* across multiple agencies, jurisdictions, and disciplines that do not always have a natural incentive to collaborate. Most obviously, rapid urbanization has caused urban centers to spread beyond city boundaries and across disparate local governments that often fail to coordinate their actions, making it difficult to take a strategic approach to managing urban growth. A lack of sufficient policy coordination similarly hinders progress on a number of other aspects of urban development. For instance, UKP-led discussions and follow-on research by Professors Paul Collier and Tony Venables on the persistence of informal settlements demonstrate that there is no one root cause that explains the failure of delivering affordable housing. Rather, success will require addressing a number of interrelated impediments through integrated action across disparate policy domains—from financing to housing regulations to the cost of construction materials—because isolated progress on any one bottleneck will be of limited impact as the others will continue to bind. For urban knowledge generators and development practitioners to help, they must lead by example by leveraging platforms like the UKP to collaborate across disciplines and sectors to build integrated solutions to urban challenges.

Third, the number one obstacle to providing city leaders with a fact-based understanding of their challenges and opportunities is the *poor quality and tremendous fragmentation of city-level data*. In fact, while many policy decisions are made and implemented at the local level, most statistical information is collected at the national level. As a result, there is today more reliable data on, say, the island-nation of Fiji—with a population of 860,000—than there is for the megacities of Delhi, Shanghai, or Rio de Janeiro, which each have populations in excess of 10 million. This creates an enormous mismatch between the scale at which information is available and the level at which urban development is conducted and significantly constrains the growth of cumulative urban knowledge generation across countries, regions, and disciplines. To address this issue and respond to the overwhelming demand of its members and participants, the UKP has partnered with the Swiss government to, for the first time, systematically bring together and visualize data on cities for global benchmarking and evidence-based decision making. The goal is to work with cities and partners to harmonize, standardize, consolidate, and open-source city data to form a robust global evidence-base on the challenges and opportunities faced by cities.

Data are the seeds of knowledge. And there is a need for much richer knowledge to help inform the decisions of city leaders. Accordingly, moving forward, the UKP aims to equip cities with the tools and guidance to become “learning cities” that leverage the tremendous advances in technology and data

analysis—from “smart city” sensors to satellite imagery— to rigorously, systematically, and openly evaluate urban projects, so that local knowledge gets transformed into evidence that can be used by cities all across the world. The World Bank through the UKP is committed to facilitating this shared learning across cities. But the Bank cannot do this alone.

The key is for the urban community to come together to build a global pool of experience and evidence that all can draw and build from to better inform the tough and often irreversible decisions that city leaders need to make to harness urbanization for sustainable development.

## **Other**

Various bilateral agencies and United Nations (UN) agencies have also undertaken initiatives to assist urbanization. Such efforts include the UN Population Fund (Box A3.3) and a joint effort by various bilateral and multilateral institutions; i.e., Cities Alliance (Box A3.4).

### **Box A3.3: UNFPA's Work on Urbanization**

**Urbanization in the BRICS – Brazil, Russia, India, China and South Africa.** UNFPA and the International Institute for Environment and Development (IIED) have collaborated for the past four years on a wide-ranging knowledge-building project focusing on urbanization in the BRICS, which provide some inspiring examples of how to seize the opportunities that urbanization can provide. All have gone through difficult periods when they tried to resist the predictable movement of people into their cities, or steered people or enterprises to inappropriate urban locations. Several of the BRICS bear heavy burdens from past failures to accommodate urban population growth equitably and efficiently. To avoid such burdens, cities and nations need to plan proactively for urban growth, making use of both markets and planning tools, and engaging with all sectors of society, including the economically and politically weakest.

**Urbanization and gender dynamics.** UNFPA also partnered with IIED to develop the conceptual and empirical foundations of the links between urbanization and gender dynamics. A recent working paper highlights the tendency to plan against, rather than for, low-income urban residents and its implications from a gender perspective. This planning does not exclude the urban poor from income-generating activities but makes it difficult for them to secure decent living conditions. In so doing, inadequate urban policies place a disproportionate burden on reproduction rather than on production activities, and on women rather than men. A gendered understanding of urbanization and urban poverty highlights how urban disadvantage also includes limited access to shelter and basic services.

**Urbanization, climate vulnerability, and adaptation planning.** In the midst of a rapidly expanding global adaptation agenda, it is of primary importance to get adaptation and its constituent parts right to generate the most appropriate and effective interventions. There is an increasing need to anticipate and reduce the suffering and the enormously damaging impacts coming events will cause. This work points to the vital role that understanding population dynamics and extensively using demographic data has in developing pre-emptive and effective adaptation policies and practices, and illuminates who is vulnerable and how to help build their resilience.

**POPClimate web platform.** Spatial analysis of population data is at the core of understanding and acting on climate vulnerability, particularly in high concentration, high exposure urban areas where vulnerability is dynamic and climate impacts threaten the lives and livelihoods of many. The POPClimate web platform was developed around UNFPA's manual on the analysis of census data for climate adaptation planning and was designed to bring together a community of data users, climate practitioners, and adaptation planners who can develop, share, and comment on new approaches for data-driven adaptation planning. The website is open to select users now and will be launched publicly in the next month ([http://nijel.org/un\\_popclimate/](http://nijel.org/un_popclimate/)).

**Other UNFPA initiatives with respect to urbanization.** UNFPA contributed to the development of the World Bank's Urban Risk Assessment methodology, particularly focusing on the importance of a dynamic understanding of risk and vulnerability that integrates urban growth and change. It is also engaged in with IIED to come up with more innovative ways to manage densities in cities and is conducting joint research in the field of urban food security.

*Source:* UNFPA 2013.

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#### **Box A3.4: Cities Alliance - A New Business Model to Promote Systemic Change and Scale**

The Cities Alliance is a global partnership whose members include multilateral and bilateral development agencies, donor and developing country governments, international associations of local government, and two international NGOs, one of which represents slum dwellers. Launched by the World Bank and UN-Habitat in 1999, the Cities Alliance was immediately successful in ensuring that the issue of slums was incorporated in the international development agenda. Today, working through the capacity of its members, the Cities Alliance seeks to: (i) strengthen and promote the role of cities in poverty reduction and sustainable development; (ii) improve synergies between and among members and partners, and (iii) improve the quality of urban development cooperation.

The larger context of CA's work is the process of urbanization that has already transformed Latin America and is now transforming Africa and Asia. Too often, this transformation is characterized as an uncontrolled and overwhelming swamping of existing towns and cities. However, the sheer scale of numbers and the pace of change should not obscure the practical steps needed to make this a manageable and even successful transition. Central to a successful transition is the need for policy makers and development agencies to acknowledge the trends, to plan for urbanization and for future growth, and to understand the process of both city and social transformation that this entails. It also points, very clearly, to the extremely high social and economic costs of failing to do so, impoverishing city and citizen alike.

Good urban policies need to be based on solid data, the generation of which the Cities Alliance has supported: from the sophisticated and comprehensive HABISP model in Sao Paulo,<sup>82</sup> which provides comprehensive information on housing and other socio-economic conditions of the urban poor, and which informs public interventions, to the *Know Your City* Campaign, which sees slum dwellers collaborate with their local governments.

To help its partners better respond to these kinds of challenges, the Cities Alliance completely restructured the organization, adopted a new Charter, and changed its business model. Moving decisively away from single, often *ad hoc* projects, the Cities Alliance used a US\$15 million grant from the Bill and Melinda Gates Foundation to move the fulcrum of its work program to longer-term, programmatic support in the form of multi-faceted Country Programs.

The combination of multiple activities in support of a coherent national program holds very real promise for the systemic change and scale impacts that the Cities Alliance is seeking to support. In Uganda, for example, that support is focused on all 14 secondary cities, which is not only where the bulk of urbanization is taking place, but also where capacity constraints, infrastructural backlogs, and affordability challenges are most extreme.

With the support of Cities Alliance members, including both the World Bank and Slum Dwellers International (SDI), the Government of Uganda is drafting a national urban policy. In small cities like Arua, Jinja, and Mbarara, slum dwellers are forming savings groups, and carrying out slum enumerations. Slum dwellers and local governments are now talking to each other, land is being made available, and basic services are being provided. A \$US130 million World Bank loan will soon start to provide much needed critical infrastructure in the secondary cities.

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<sup>82</sup> [www.habisp.inf.br](http://www.habisp.inf.br)