

ETHIOPIA URBANIZATION REVIEW

An Overview

March 2015

Outline

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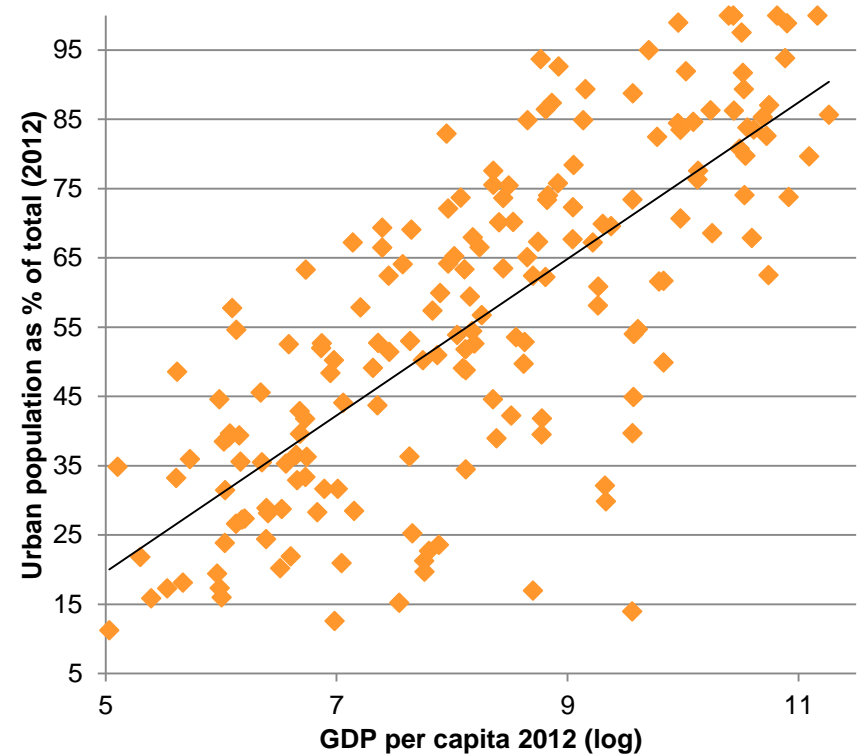
URBANIZATION

The Fundamentals

Urbanization is associated with economic growth

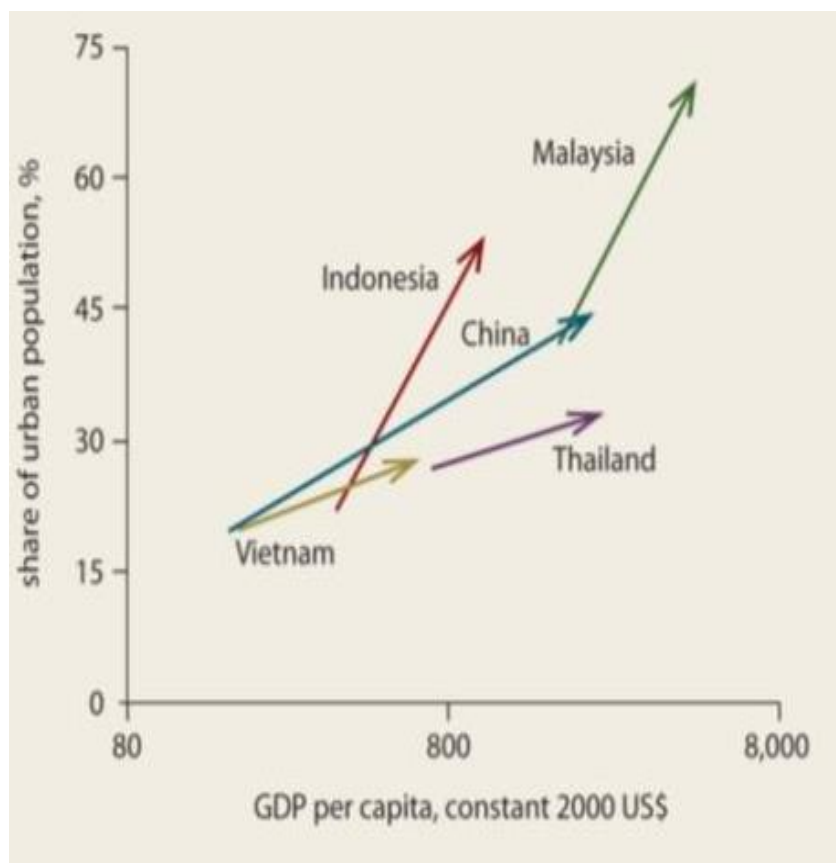
All countries achieving middle income status **have urbanized significantly**

More urbanized countries have **lower poverty** and are **more prosperous**

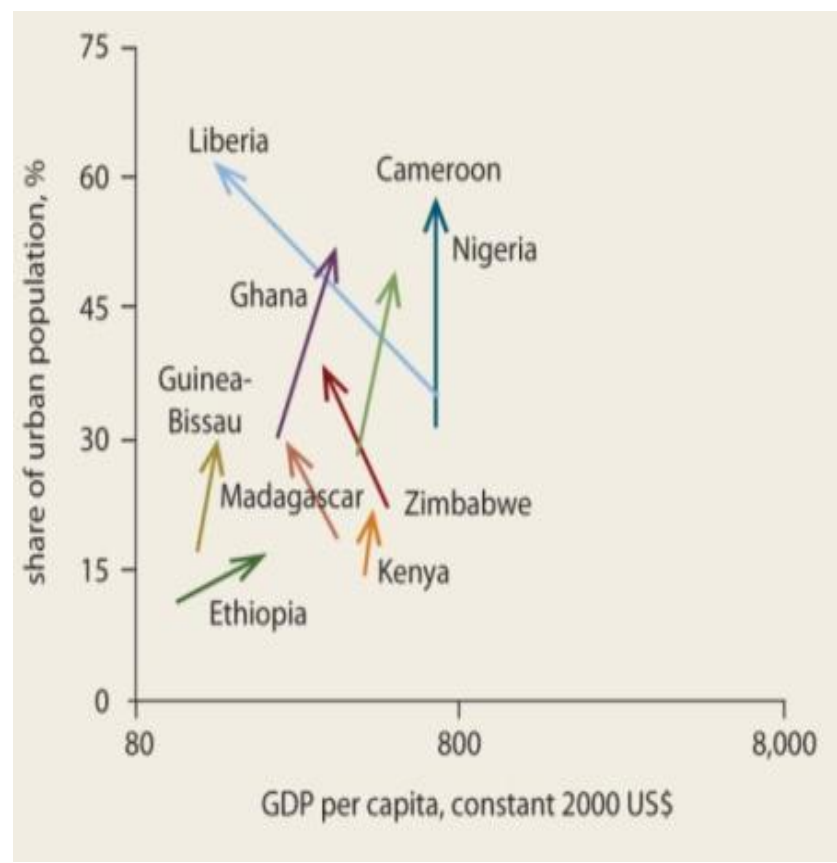


But a positive relationship with economic growth is not automatic

East Asia and Pacific



Sub-Saharan Africa



The management of urbanization is vital

The concentration of population in urban areas provides the opportunity to deliver basic services at scale—and decreased cost

- On average, piped water is \$0.70-0.80 per cubic meter in urban areas compared with \$2 in sparsely populated areas (GMR, 2013)

However urbanization on its own is no guarantee of success

- While urbanization holds the prospect of driving economic growth, reducing poverty, and expanding access to jobs, housing and services for an increasing share of the population, much depends on HOW the process is managed.

While all countries urbanize, not all profit equally

- Some do so well, and capture its benefits
- Some do so poorly and are left with cities which are characterized by slums, congestion, pollution and do little to support growth

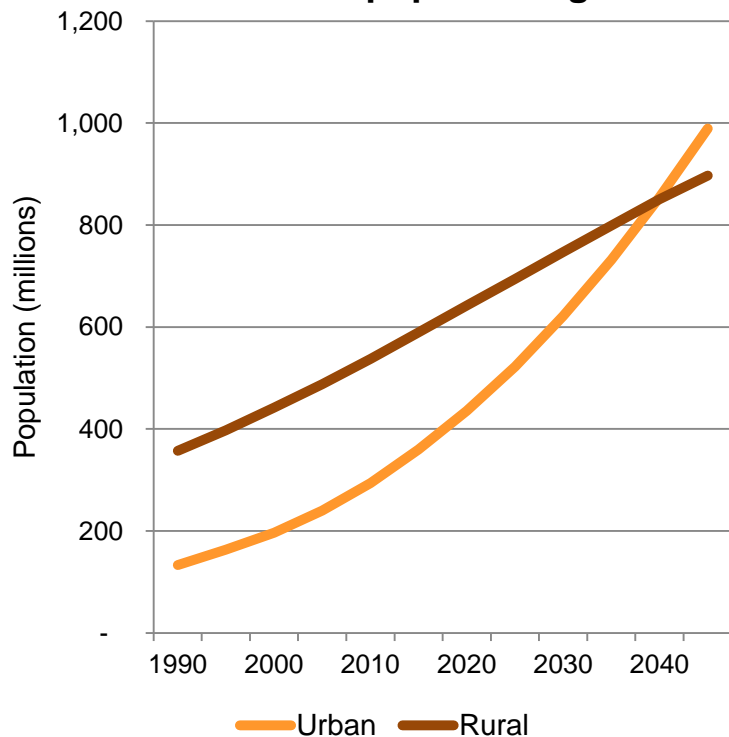
URBANIZATION IN AFRICA

The Trends

Africa is urbanizing...

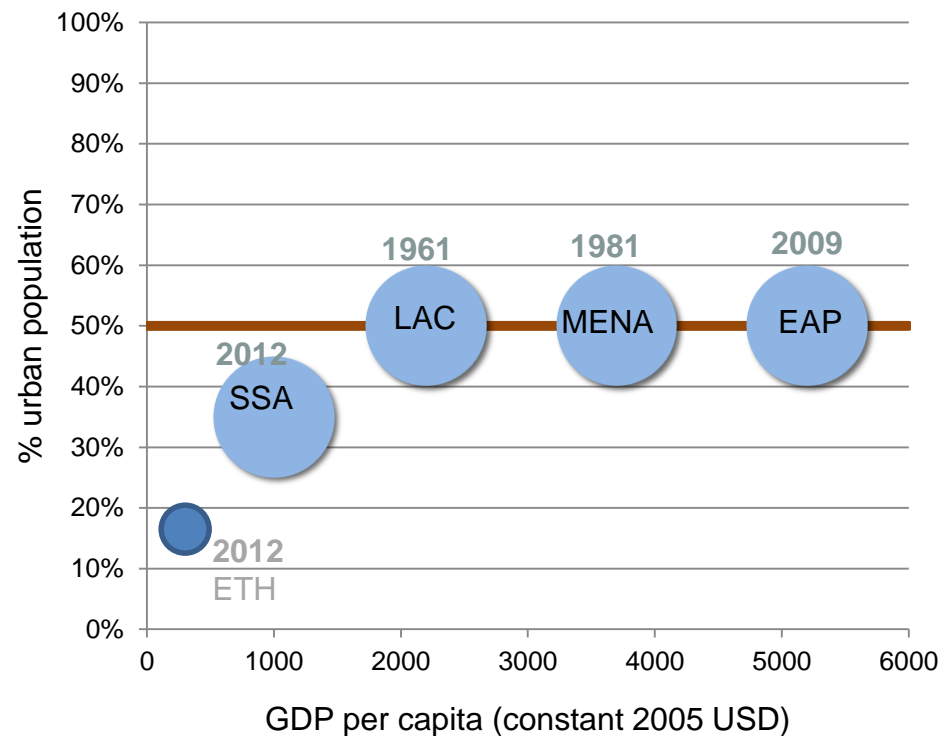
Very rapidly...

African population growth

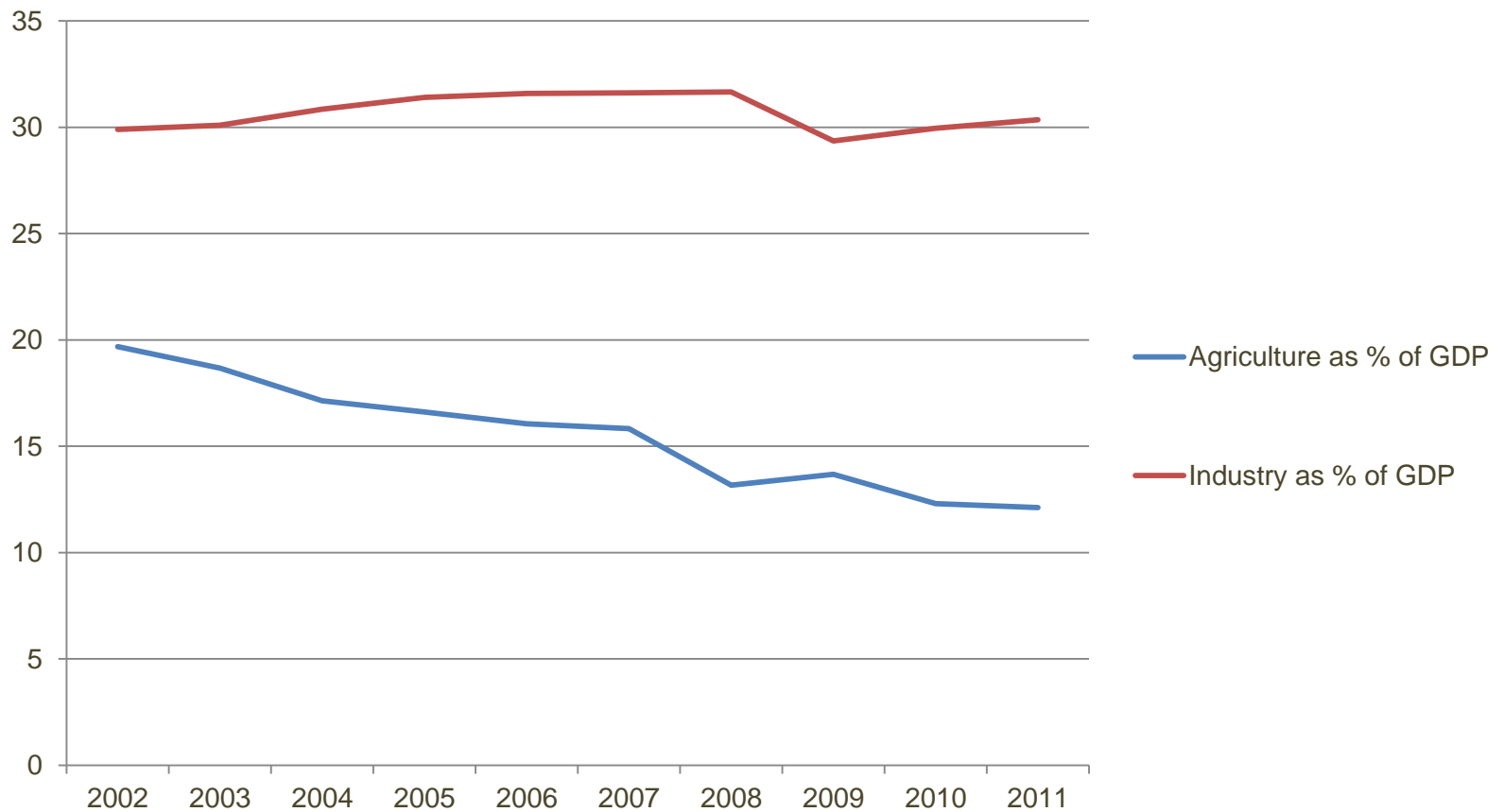


but late and at low incomes

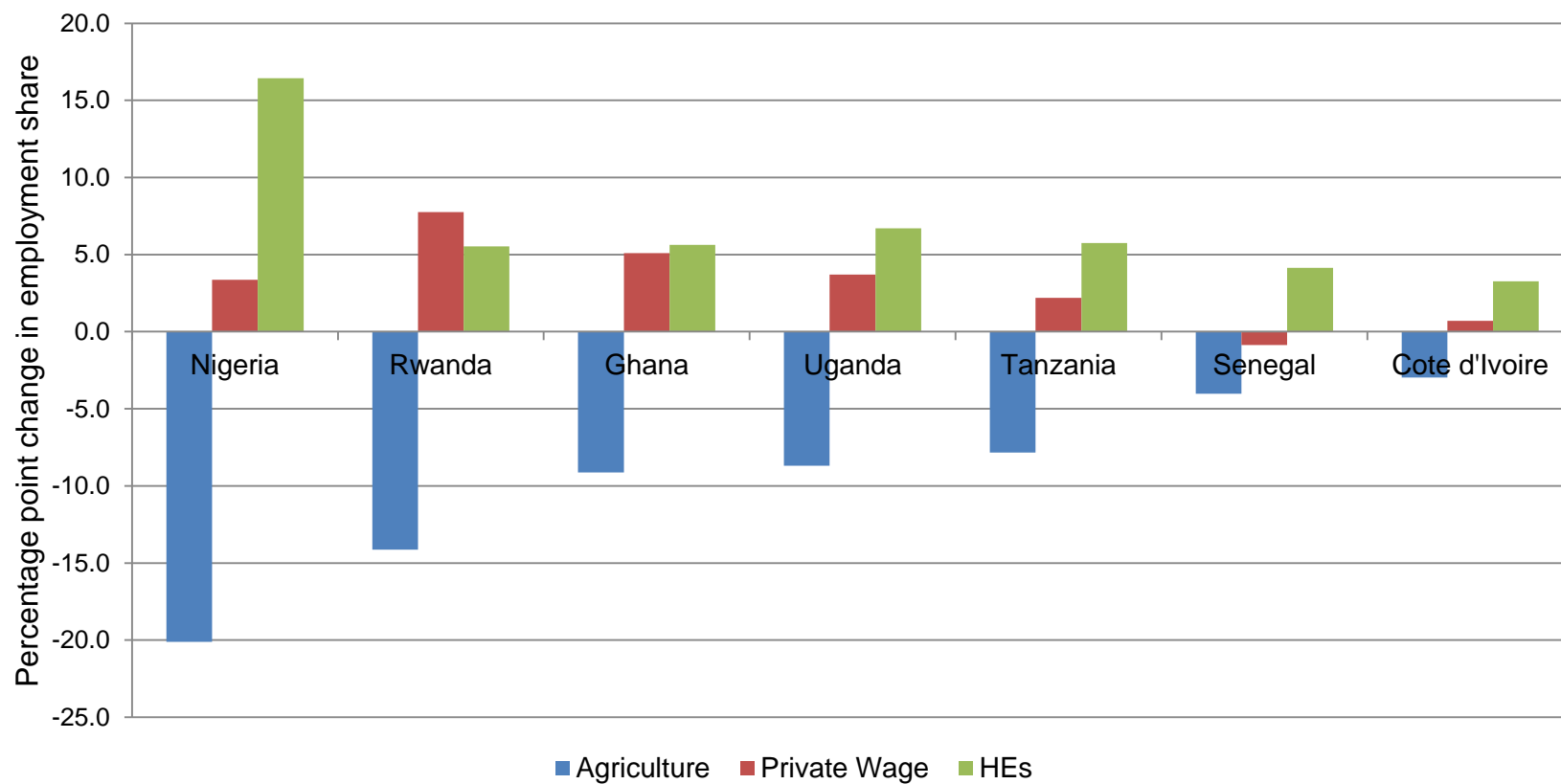
Income and year of shift to urban majority



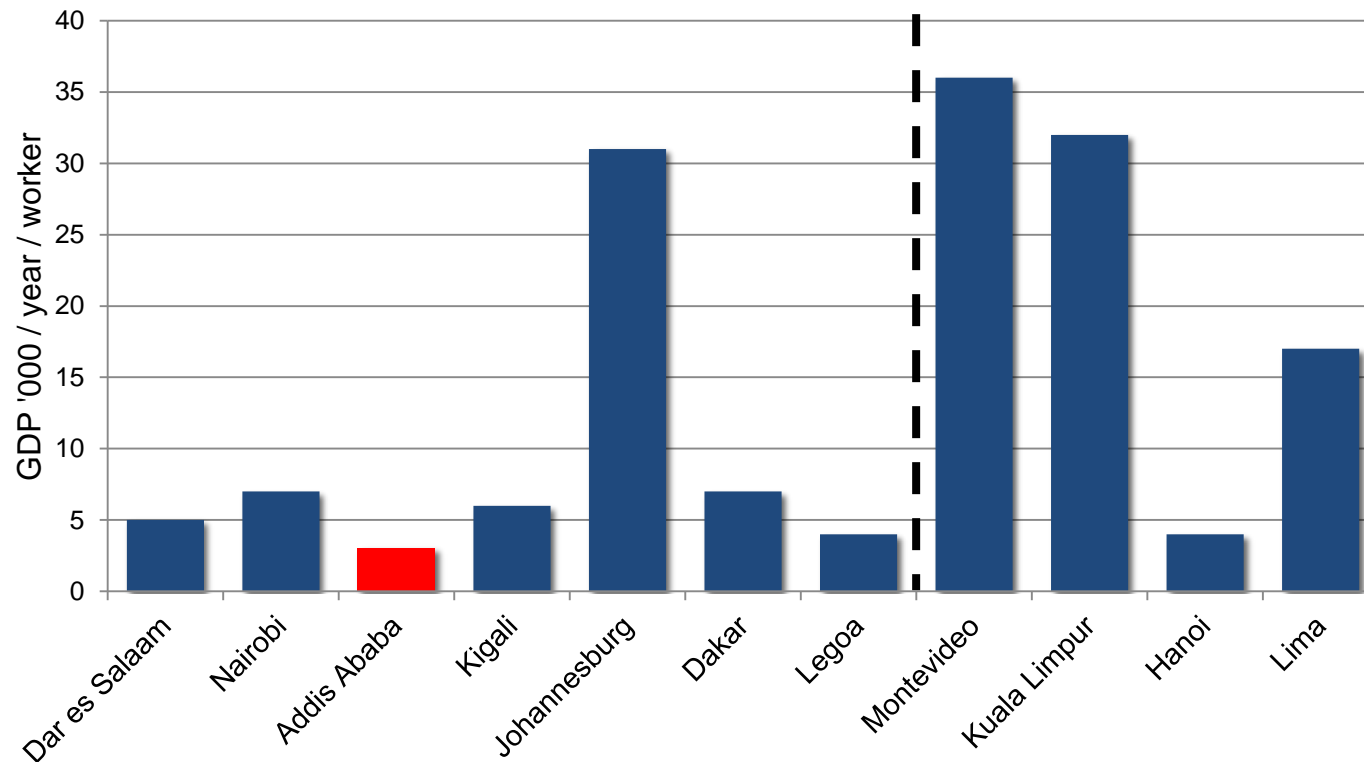
Africa's economies are increasingly urban..



And so are its jobs

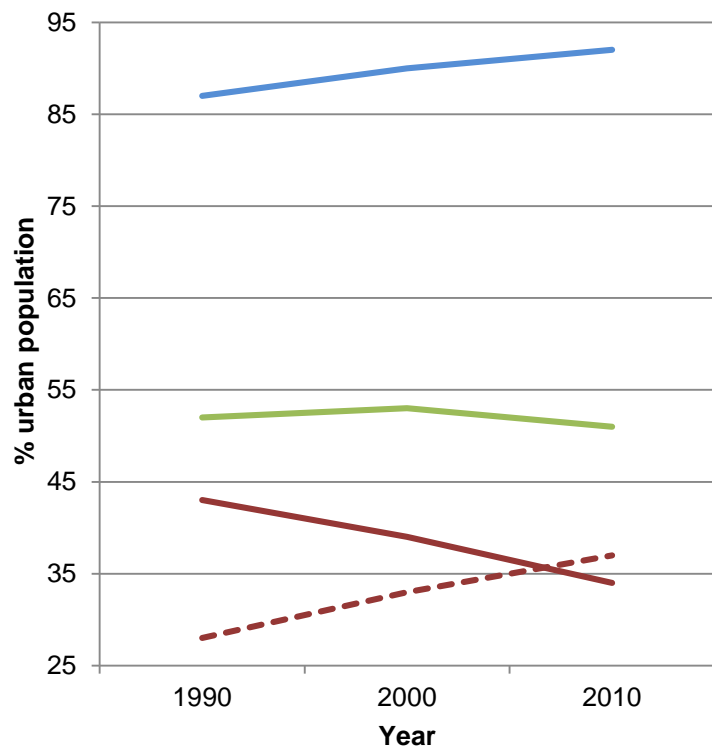


Africa's cities are not very productive

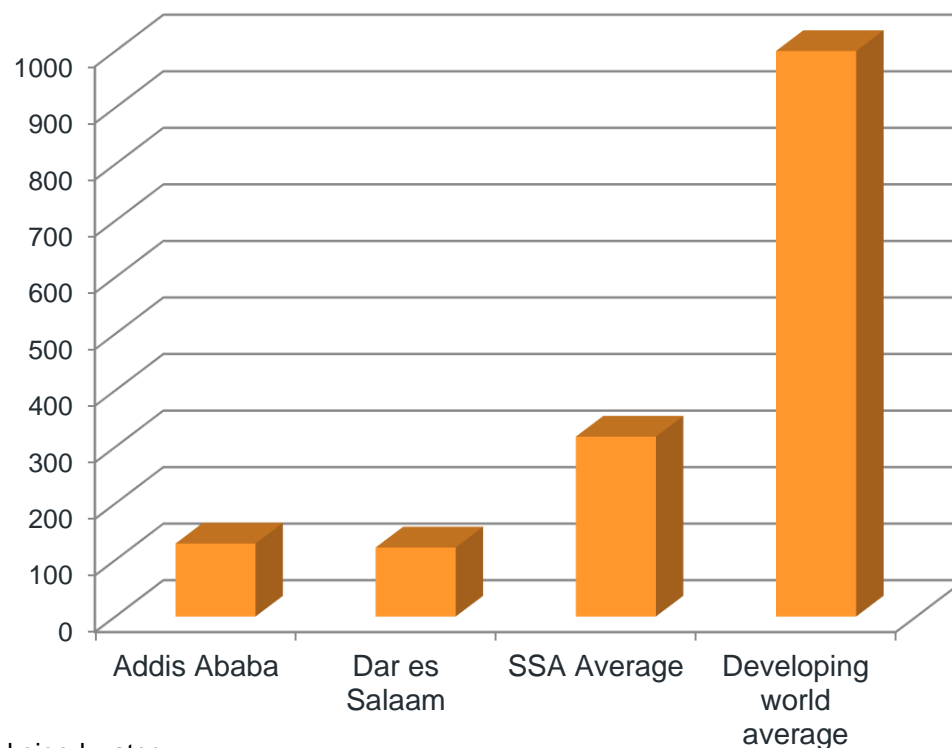


And service-delivery is struggling to keep up...

Water supply coverage (%)



Paved roads (m per 1,000 people)



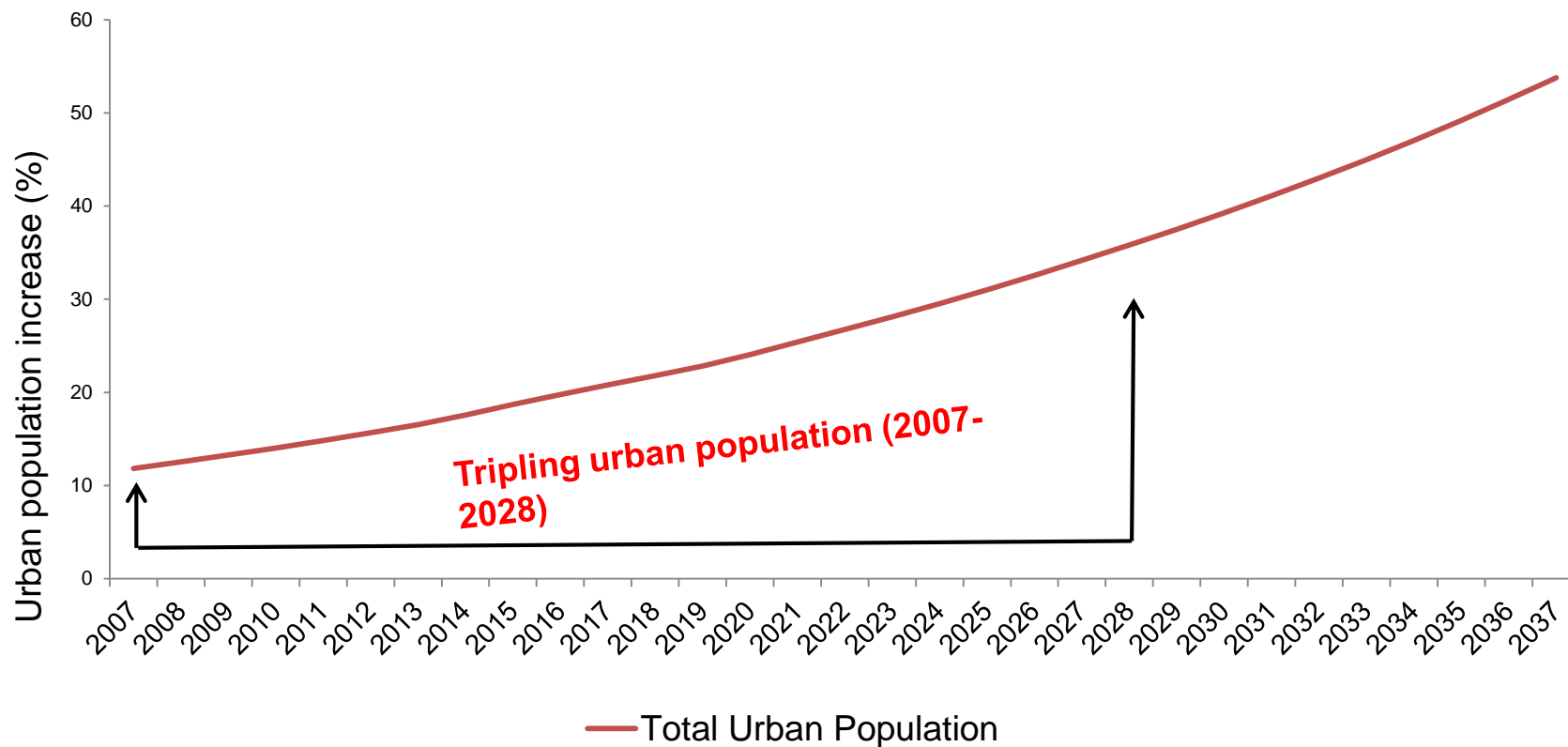
- Sub-Saharan Africa - % of urban population using improved piped water
- South Asia - % of urban population using improved piped water
- LAC - % of urban population using improved piped water
- - - Sub-Saharan Africa - % urban population

URBANIZATION IN ETHIOPIA

A One-Off Opportunity

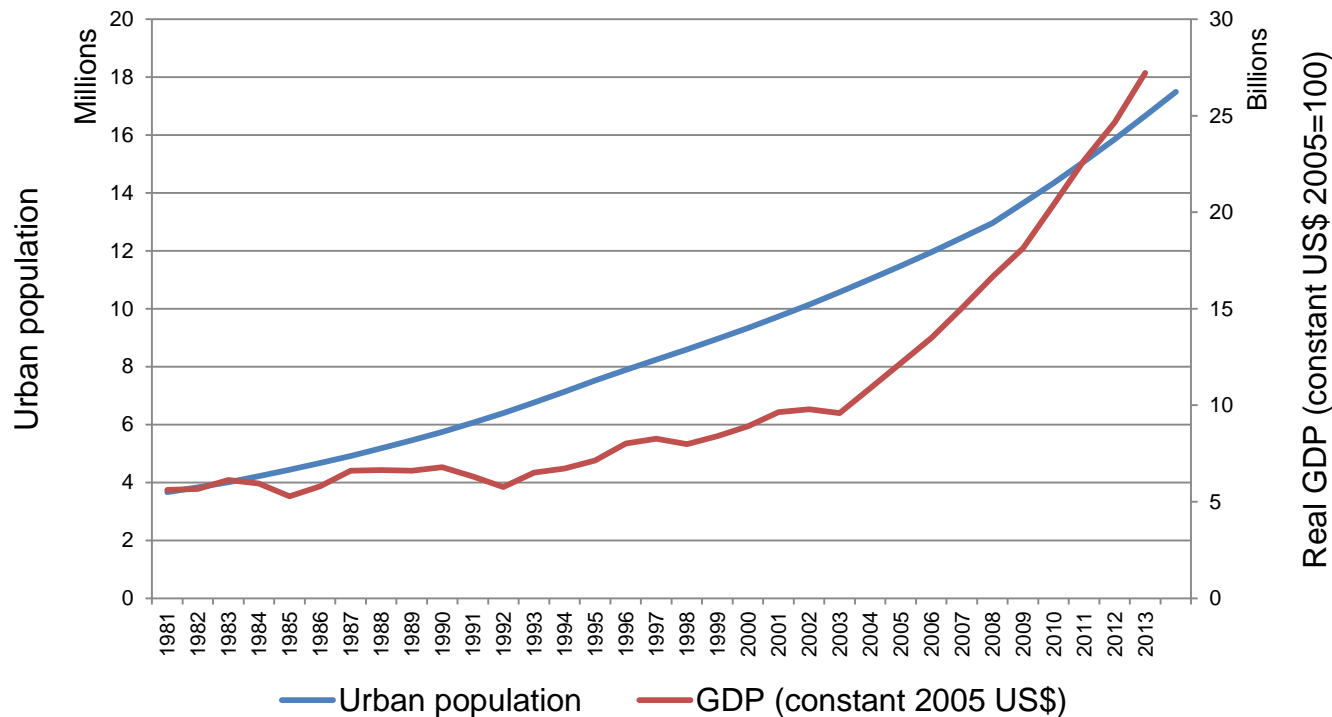
Section I: Urbanization and Economic Growth

Ethiopia's urban transition has taken off

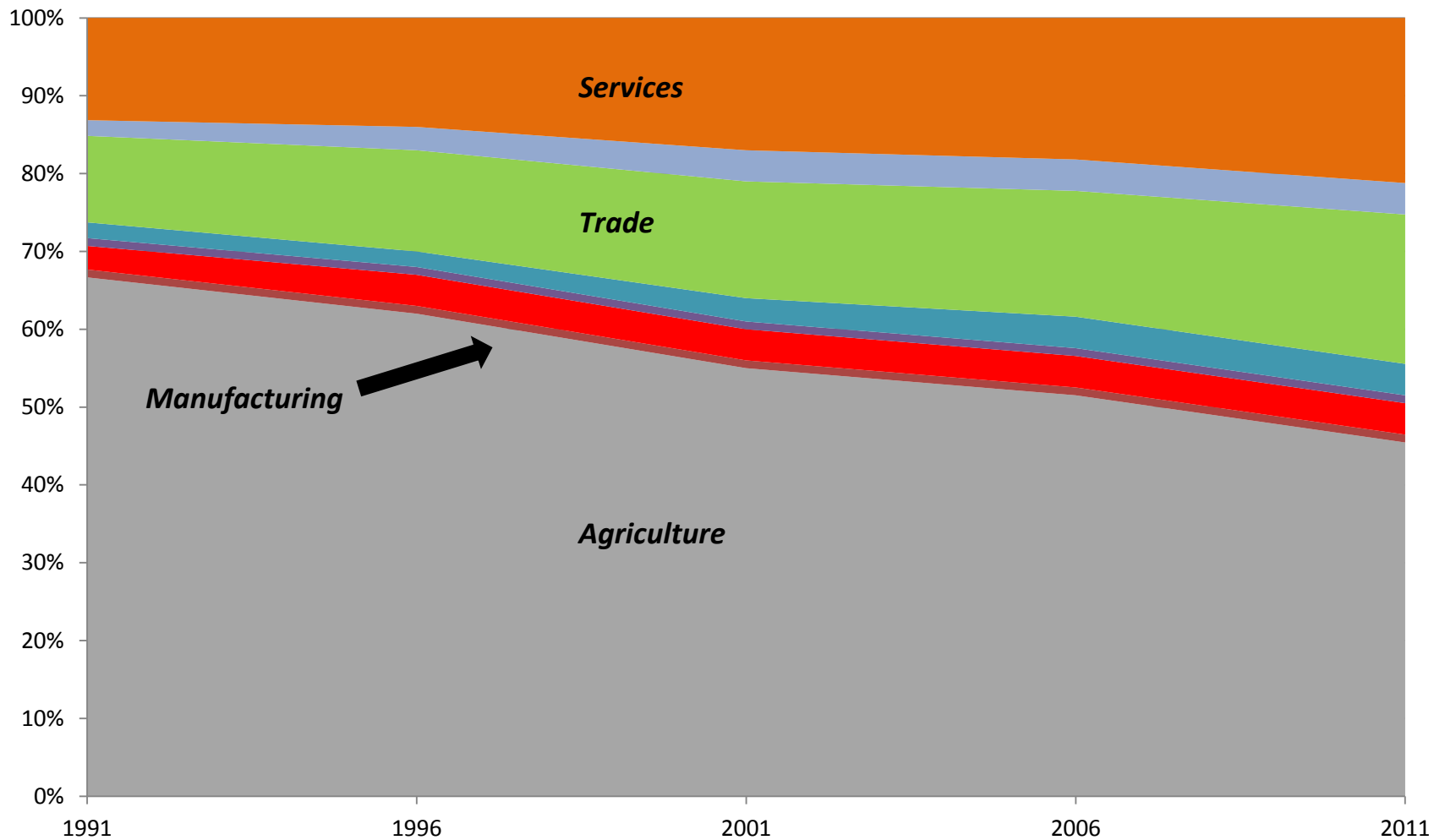


Ethiopia's urbanization is associated with economic growth

- As in other countries, urbanization in Ethiopia has been associated with **high levels of economic growth**, averaging 10.4% between 2003 and 2013.
- **Cities contribute to 38% of GDP** with only 15% of total workforce.
- Assuming sustained high growth rates, **Ethiopia could reach middle income status by 2030** (GNI per capita \$1,560)

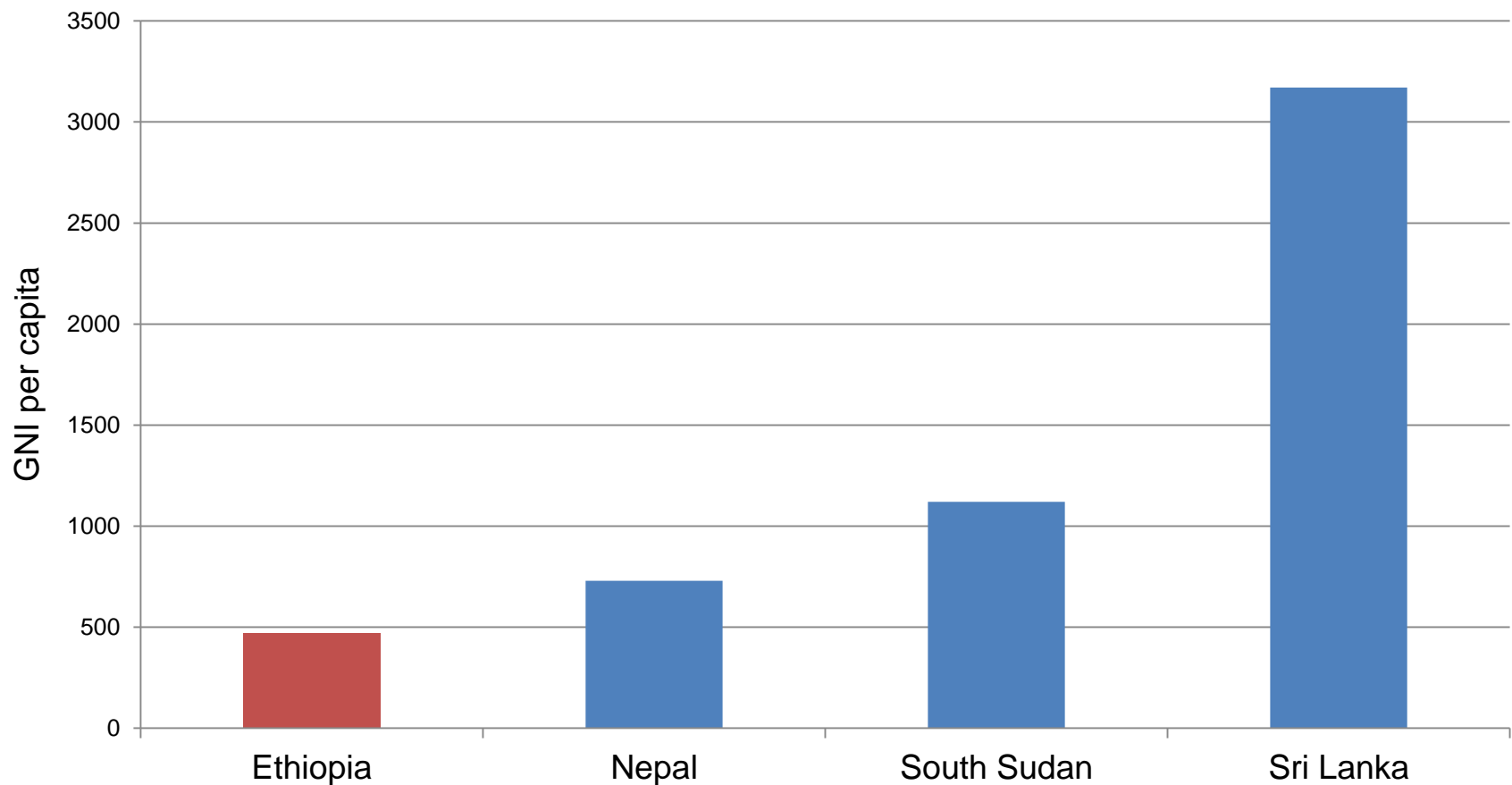


But structural transformation has been modest



Ethiopia not maximizing returns from urbanization

Ethiopia has a lower level of GNI per capita compared to other countries at 18% urbanization



URBANIZATION IN ETHIOPIA

A One-Off Opportunity

Section 2: Priority Areas for Investment

Three core priorities

Urbanization needs to be managed proactively, otherwise cities will struggle to provide jobs, infrastructure and services, and housing.



#1 Jobs



**#2 Infrastructure
and Services**

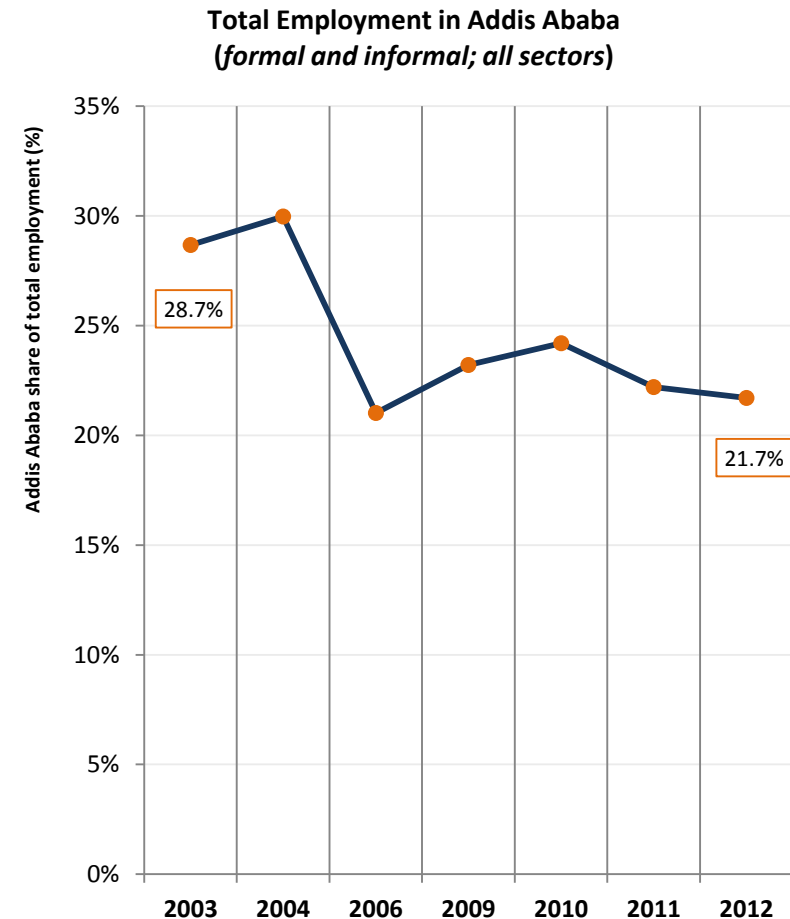


#3 Housing

Job creation is lagging

Ethiopia has higher than average unemployment

- **Ethiopia unemployment** (15% in urban areas) is higher than other SSA countries
- **The informal sector**, which provides most employment in SSA, is lower in Ethiopia (37%) than in SSA (60%)
- **Manufacturing employment** only accounts for 3% of total employment
- **Most jobs are in firms that are small**, or in self-employment but these firms tend to stay small
- **Addis' primacy** in job creation is declining



Continued economic expansion, will require structural transformation, and more urban economic development

Growth in Ethiopia has been associated with an increase in value-addition in services, but with modest structural change and little industrialization.

- **Growth has been driven primarily by public investment and agriculture**, but agriculture has begun to decline substantially and the services and construction sectors have begun to expand
- **Manufacturing contributes a small share** of a rapidly expanding economy, although manufacturing jobs are concentrated in cities
- For the shift away from agriculture to industry and services to be accelerated, and for rapidly growing urban populations to be accommodated, **urban competitiveness and liveability need to be enhanced**
- **Cities need to function better**: a wide-ranging policy, institutional and investment agenda is required...

At the policy level...

Some steps are being taken to target job creation

- **Micro & Small Enterprise Development Agency:** 83,000 MSEs and almost 75,000 new jobs created between 2004-2009
- **ULGs facilitate transition to formality** through targeted development
- **Secondary cities** are getting good at attracting economic activity, forming industrial clusters, notably Adwa, Sebeta, Bishoftu, Adama, Hawassa, and Mekele

However...

- **Ethiopia has a 'missing middle' of firms:** Government support is geared mainly towards new firms, but growing firms need more attention
- **Urban local governments have more responsibilities** (following city proclamations), but require additional capacity to implement their new remit
- **The links between formal and informal, and waged and self employment are not well understood or coherently addressed:** A number of programs target self-employment; at the same time, informal activities are often penalized

International experience suggests

- **Primarily waged employment** leads to the emergence of a middle-class
- **Informal sector** accounts for a growing proportion of jobs in SSA economies
- **Only sustained increases in nonfarm employment** can help lead to structural transformation.

...but more job creation is needed

Micro and informal sector enterprises

- **Light-touch**, supportive regulation of household enterprises
- **Support small-scale facilities** which promote access to customer bases and supply chains
- **Support the development of small-scale businesses** in sectors which have significant potential and can expand symbiotically with formal sector enterprises e.g. taxis, “boda boda” motorbikes feeding BRTs

Small & Medium Enterprises

- **Expand ULG capacity** to administer improved local business licensing and permitting systems
- **Extend support** currently provided to start-ups to existing firms to expand
- **Monitor local constraints** and track impact

Targeting Large Enterprises and Investors

- **Improve** licensing, permitting and tax systems
- **Expand** supply of serviced land & infrastructure

Major investment in infrastructure and services is required

The rapid growth of people and jobs in urban areas means large new needs for serviced land and infrastructure in cities

- Strategic infrastructure, such as roads, water, electricity, solid waste management, etc., and well located land needed for rapidly expanding urban population and businesses

Significant progress in last two decades as a result of government interventions

- Despite progress, much remains to be done to satisfy present levels of demand
- Addis Ababa only city with municipal sewerage, which serves only 10% of the population.
- Solid waste management remains a challenge often dumped into open areas, endangering public health.
- Road density is below African average, although higher in urban areas than country as a whole
- Water provision especially challenging—low rates of per capita consumption. And population growth plus increasing per capita consumption would require significant increase in water supply

There are serious housing challenges

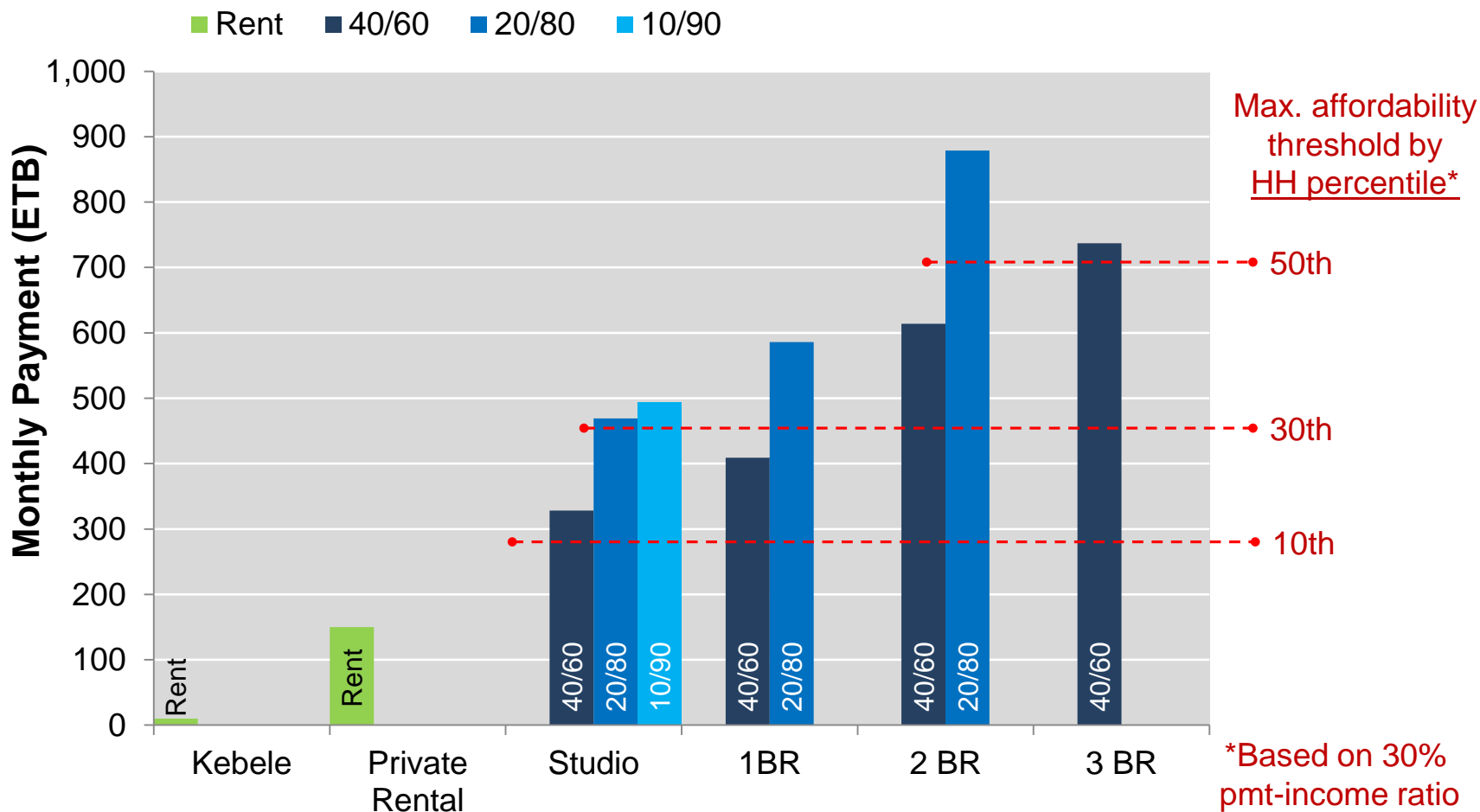
Supply

- There is a chronic housing deficit in urban areas, both for the un- and under-housed.
 - very poor quality structures (78% in slums, 66% with dirt floors)
 - lack of basic infrastructure (73% urban pop lacks improved sanitation)
 - high share of urban households living in housing not recognized by the government

Affordability

- Data indicate that the cheapest formal housing options are only affordable to the middle and upper income groups
- Rental (kebele and private) is most affordable option for poorer households.

Affordability of IHDP in Addis Ababa



Policy interventions have limited effectiveness

- **Government of Ethiopia acknowledges these important challenges** and has responded in the following way:
 - Local governments: Land allocation for housing
 - Federal response: Integrated Housing Development Program
- **IHDP provides large subsidies to a small portion of the urban population**
 - Does not address widespread housing needs, particularly of low income groups; only meets 10% of estimated need (40k units per annum vs. 400k needed)
 - Financially unsustainable for government (estimated 50% subsidy per unit)
- **Local government land allocations:**
 - Land lease revenues are well below cost of providing serviced land, which results in a significant undersupply of residential land

URBANIZATION IN ETHIOPIA

A One-Off Opportunity

Section 3: Urban Institutions for a Middle Income Ethiopia

Urbanization is a one-off opportunity

Urbanization in Ethiopia is a one-off opportunity to connect people to prosperity and reach middle income status by 2025

- Ethiopia has to get its urbanization “right”: the policies, institutions, and investments put in place now will influence urban systems for years to come: once the urban structure is set, it is very costly to retrofit

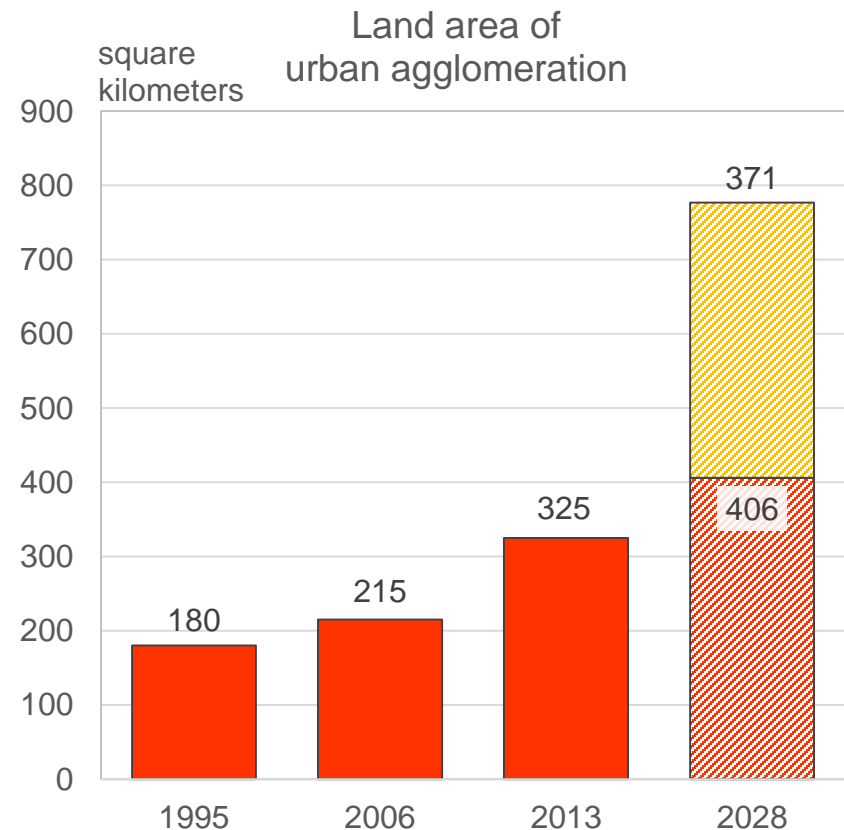
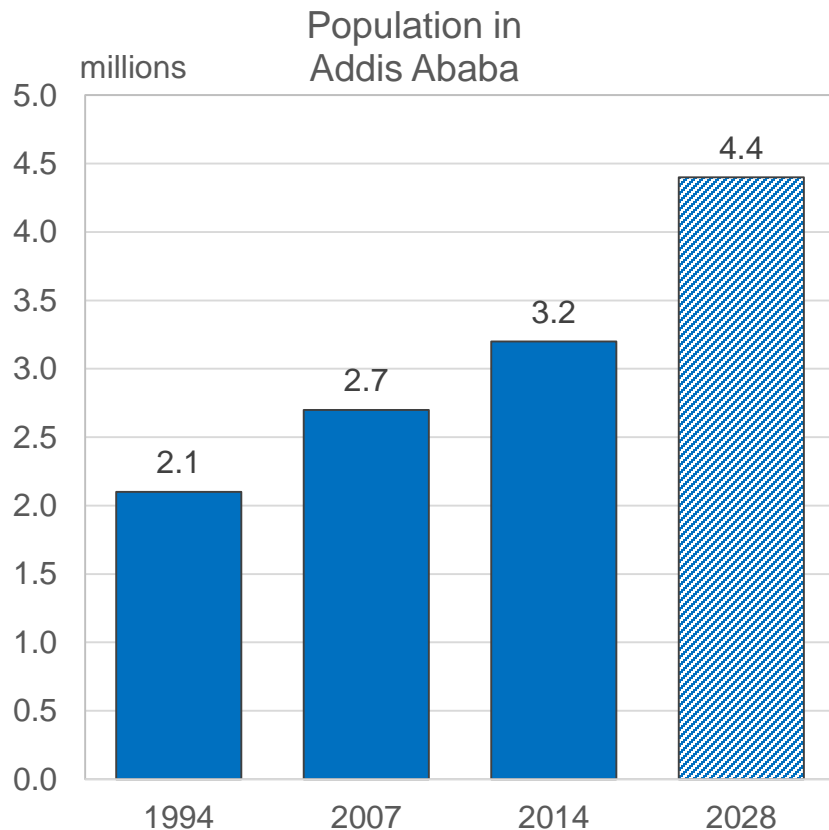
What is needed

- In order to tackle the three priorities of jobs, infrastructure and housing, critical reforms to urban policy and institutions are needed in the areas of land, urban financing and management
- This needs to be backed by a strong coalition of federal, regional, and local governments and adequate resources.

The government has already taken steps to make evidence-based, informed decisions for well-managed urban growth, and this work aims to contribute to those efforts.

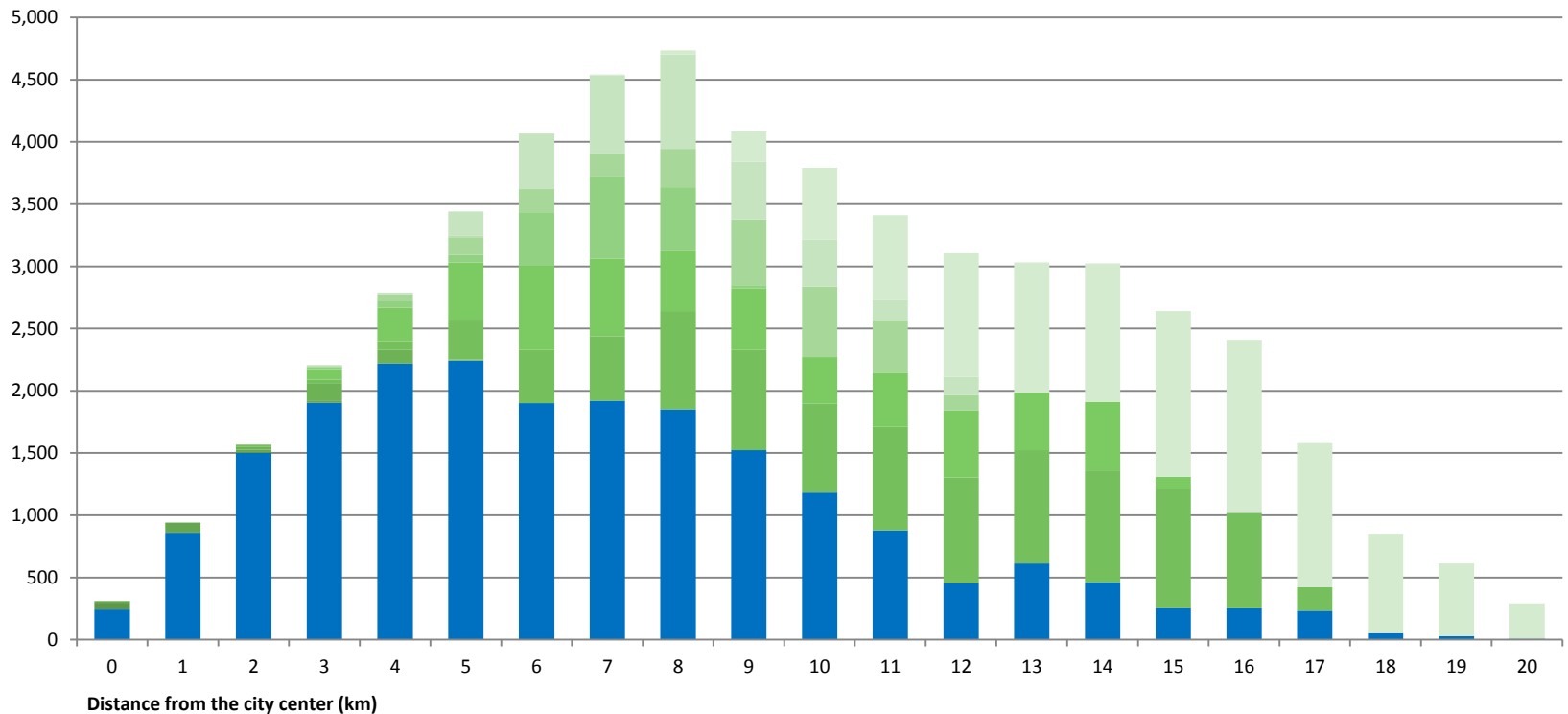
Urban land consumption is increasing fast

Cities are growing faster than population growth, driving up the costs of infrastructure and service delivery.



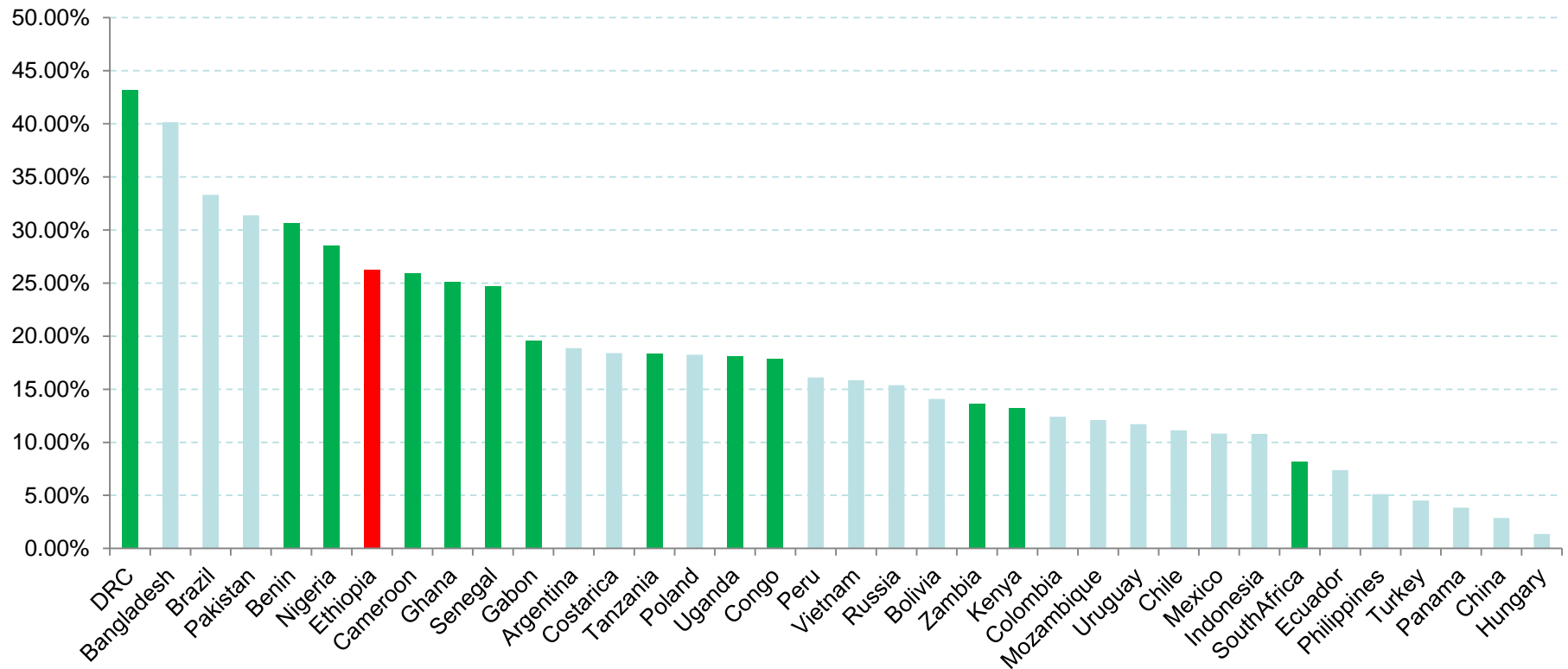
Many Ethiopian cities have vacant or underused land in prime locations

Vacant, buildable land in Addis Ababa



Urban land constraints hamper investment

% of surveyed firms who rate access to land as a major or severe constraint to doing business



Source: World Bank Enterprise Surveys, various years 2006-2013. Ethiopia survey, 2011. Manufacturing firms 22%, Services firms 34%.

A number of changes are proposed

Land recommendations

- Simplify the urban land leasing system and make lease rights more tradable to encourage private sector investment and to lessen the administrative burden on ULGs
- Use multiple land allocation mechanism and diversified pricing of land to generate greater revenues for investment in infrastructure and allow for cross-subsidization

Housing recommendations

- Focus available fiscal resources on provision of land and infrastructure for low-income groups and slum upgrading
- Support affordable housing delivery and household investment in dwellings through relaxing housing standards and allowing incremental housing consolidation

Limited authority and capacity of ULGs hampers urban management

- In Ethiopia, city proclamations have endowed **city governments with increasing powers**, leading to economic convergence across cities and falling spatial inequalities.
- **Strengthening cities' administrative capacity** has proven to be a critical enabling factor for attracting and retaining firms and creating jobs.
- At the same time, important **powers in practice**—such as tax and tariff setting authority— are maintained at the regional level and this hinders the urban areas' ability to provide jobs, infrastructure and services
- And ULGs have **very limited planning, project execution and administrative capacities**

Two sets of measures are required

Reform institutional structure of urban local government to expand ULG autonomy such as:

- Powers to determine their own structures and attract the necessary human resources

Build capacity through strengthening systems and enhancing human resources in areas such as:

- Planning
- Project execution
- Financial management and procurement

Urbanization is significantly under-resourced

ULGs have been allocated very limited own sources of revenues, but these revenues are supposed to finance most urban development expenditure

- Municipal revenue is estimated to be only 3% of the total government revenue

With some development partner-funded exceptions, intergovernmental transfers are limited to funding operating costs – often insufficiently

In essence, there is a basic disconnect between the fiscal needs and the fiscal resources of ULGs: urbanization is inadequately funded

- Total urban development spending is estimated to be less than 4% of total government spending

Significant steps are needed

Federal Government

- **Increase investment** in urban development through expanded fiscal transfers
 - Invest in key strategic infrastructure and services for Addis
 - Expand coverage of secondary cities
- **Expand ULG revenues** through developing policy focused on increasing land-based revenues and property taxation
- **Fiscal Review** periodically analyze intergovernmental finances (e.g. South Africa's Intergovernmental Fiscal Review).
- **Clarify mandate** for the federal agency responsible for guiding and supporting local revenue enhancement

Regional governments and ULGs

- **Incentivize improved local revenue collection** by allowing them to keep state revenues generated in excess of targets
- **Expand ULG control over rate levels for OSRs** such as user fees and land rents
- **Enable ULGs to** (i) recover true cost of services through user fees and (ii) introduce inflation adjustments for municipal fees and charges

URBANIZATION IN ETHIOPIA

A One-Off Opportunity

Section 4: Takeaways

Takeaways

Rapid urbanization brings with it **important opportunities**

Yet to realize these opportunities, urbanization needs **proactive management**

Much progress has already been made, which is encouraging

But urbanization needs to be made a national priority if Ethiopia is to reach middle income status sooner rather than later

Annex: Differentiation of land allocation mechanisms and pricing

