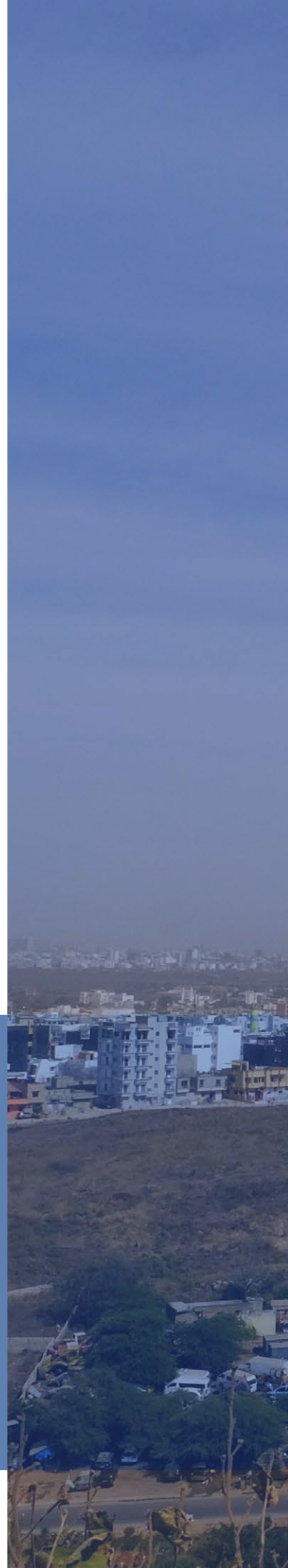


3

Anchoring the role of cities in national economic planning

This chapter outlines how important it is to draw up a roadmap for the future of cities in national economic strategies. Co-ordinating and designing policies at both the national and the local level is vital for every region of a country and every sector of the economy. The chapter offers an overview of several aspects of national policy that national governments can consider to support and boost the economic performance of cities and, in particular, it emphasises the importance of investing in human capital, infrastructure and public institutions. The final section of the chapter describes a variety of policy packages and measures that governments can draw upon to bring cities to the forefront of national economic policy.





In Brief

Anchoring the role of cities in national economic planning

National governments should anchor urban policy in economic planning, because urbanisation and economic development are closely intertwined. Cities are responsible for most economic growth and job creation in almost all countries. Their economic performance plays a crucial part in national economic success, and this is only likely to increase as urbanisation progresses. This chapter presents a set of key considerations for policy making on the economic role of cities, and a framework with thematic entry points and policy recommendations¹ for incorporating their role in national economic planning.

Targeted and coherent policies for cities are important because many national policies have spatially diverse effects, and their impact on cities is different from their impact on rural areas. Governments must consider this diversity and ensure that national policies are appropriate for fast-growing cities. Urban development requires large investments and involves multiple actors and financing sources. Well-designed national development plans can co-ordinate a multitude of actors and objectives and ensure that the economic development of cities is appropriately supported.

The number and quality of jobs that urban centres create and the productivity levels of their firms and workers determine their economic contribution. To strengthen the economic performance of cities in Africa, policy makers need to address several dimensions:

- On average, Africa's largest cities are the most productive, but their high cost of doing business and elevated cost of living reduce their economic competitiveness and the living standards of the population. This is a sign of agglomeration diseconomies that are caused by under-planning and underinvestment.
- Human capital is one of the most important determinants of productivity, especially in urban areas. Workers in large cities benefit more from high skill levels than workers in small cities. Conversely, highly skilled populations increase the agglomeration economies that cities can generate.
- Infrastructure at the local and the national level matters for economic development. The empirical evidence is strongest on the importance of a stable electricity supply, but many other types of

infrastructure, such as transport, information and communication technologies (ICT), and water and sanitation, also have important consequences for economic performance. Significant increases in public investment are needed, but such investments within a city need to be co-ordinated across policy sectors and across levels of government if they are to be effective.

- Institutions and the regulatory environment are key conditions for productivity in cities. Smoothly functioning institutions and predictable regulatory environments give firms the certainty they need to make investments. Likewise, good institutions and regulations make it possible, among other things, to secure finance and acquire land, enforce contracts and protect innovations. This is essential if firms are to grow and to increase their productivity.
- Urban form affects many drivers of agglomeration economies, such as the accessibility of jobs and firms' proximity to each other. However, few rigorous empirical studies on their importance in Africa exist and further research is needed to quantify the effect of these factors on the continent.

African cities have to provide jobs for a rapidly growing number of workers. Governments thus need to facilitate a job-rich urbanisation. Job growth in low-productivity sectors such as unskilled services runs the risk of stalling productivity. To avoid this outcome, growth in manufacturing and tradeable services, and in sectors that can deliver both job growth and productivity growth, is essential for urban economies.

Investing in the most productive cities, including primary cities, should be a priority for maximising agglomeration economies. At the same time, to redress spatial inequalities, well-targeted investments are needed in mid-size cities, as well as infrastructure that connects cities of different sizes. Policies that focus on the role of small cities with populations under 50 000 are also essential. Investments need to include human capital development and social protection, as well as sectoral policies to better match sectoral needs with preferred urban locations, and to enable firm and job churning through factor mobility between cities.

Beyond any individual policy, national governments need to ensure a coherent policy environment

for urban areas. Policy packages are generally more effective than isolated policies, because they can generate complementarities and address bottlenecks. Public

policies thus have to be co-ordinated across sectors and levels of government.

Why should national governments integrate cities into national economic plans?

Africa is urbanising at unprecedented speed. In 1950, just 13% of the population lived in urban areas. By 2015, this had risen to over 50% (OECD/SWAC, 2018^[1]). Urban areas generate a majority of GDP, are centres of innovation, and connect African countries to other economies in Africa and the world. Cities are at the forefront of social, environmental and economic development. Planning for their growth and embedding their potential in national economic planning will ensure that cities propel African countries into a sustainable and more equitable future.

Urbanisation provides a unique opportunity for economic development. The shift of labour from low-productivity rural economies to high-productivity urban economies dominated by manufacturing and services has been a key feature of economic development across the globe. The productivity advantages of cities are reflected in income levels that tend to be higher than in rural areas. However, urbanisation is associated with economic growth and structural transformation not only in cities, but also in rural areas. Without urbanisation, no rural areas have reached high income levels. As people move to towns, rural living standards can rise, because the remaining rural inhabitants have more land on which to work, and can earn more as they service the rising urban demand for food (Collier, 2017^[2]).

The positive impact of urbanisation on economic development will only be realised, however, if urbanisation is accompanied by appropriate national policies

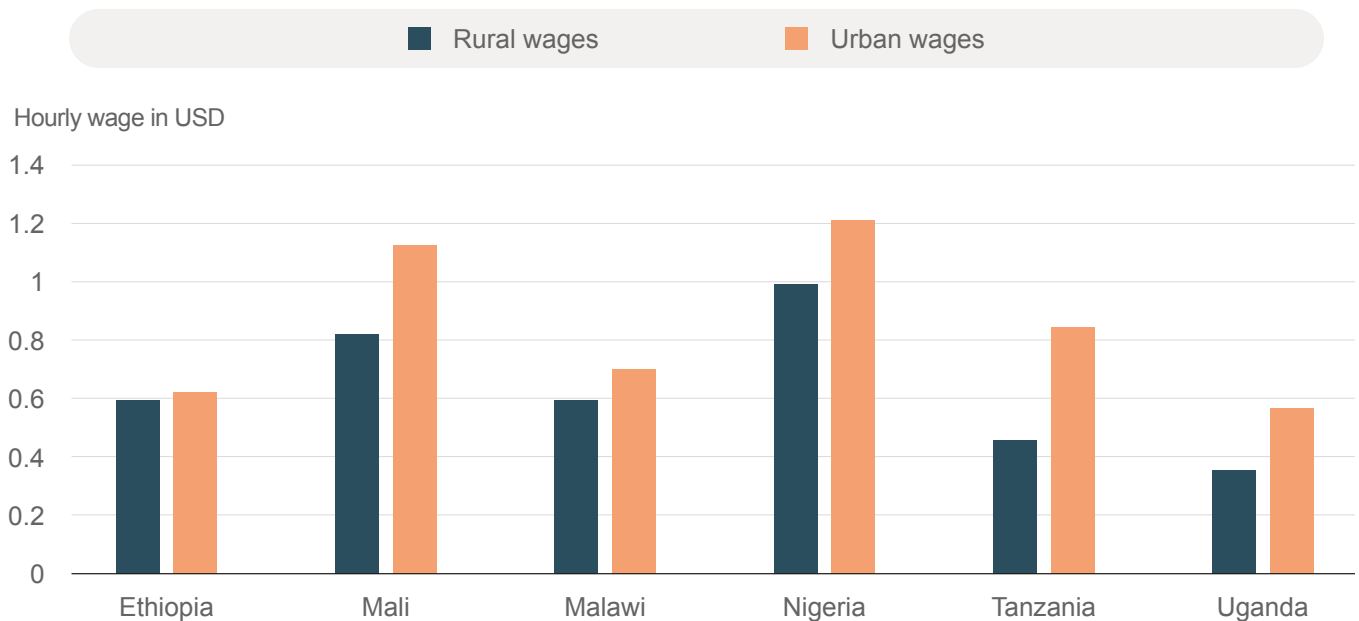
targeted at cities. Integrating cities into national economic planning is imperative, for three compelling reasons: 1) urban productivity is critical to Africa's economic growth and job creation; 2) economic policies have a strong spatial impact, which needs to be anticipated and co-ordinated; 3) urban investment is sizable, multisectoral and long term; this is complex and should be co-ordinated at the national level.

Urban productivity is critical to Africa's economic growth and job creation

Investing in fast-growing urban areas is strategically important for countries, because boosting urban economic development boosts national economic growth. As countries urbanise and economies transition, economic activity that drives national economic growth will increasingly become concentrated in cities, and as a result, economic growth will be determined by urban productivity. The more urbanisation progresses, the more important the performance of the urban economy becomes for national economic performance.

No country in the world has ever turned into a high-income economy without urbanising. Only urban economies can support the strong manufacturing and service sectors that are the backbone of advanced economies. Cities provide the pools of skilled workers, customers and suppliers, as well as the infrastructure that large firms need to operate efficiently. Moreover, cities can create jobs for growing populations, in contrast to rural areas, where labour demand in the agricultural sector often stagnates or grows only slowly.

Figure 3.1. Urban and rural wages in six African countries



Note Based on data from 2010-2019. Due to cross-country differences in survey methodologies, wage levels are not comparable across countries, but the rural-urban wage gap within each country is consistently estimated.

Source OECD/SWAC calculations based on World Bank LSMS (2008-2019_[3]) and OECD/SWAC (2018_[1]).

The advantages of cities for a modern economy are reflected in agglomeration economies and the urban wage premium. Firms and workers in cities are more productive and workers earn higher wages. However, it is important to note that urbanisation does not occur at the expense of rural income levels. In fact, the opposite is typically the case. As the available labour supply for agriculture declines, due to urbanisation, rural wages rise and capital investment in the agricultural sector becomes more profitable, thus leading to higher productivity. Moreover, urbanisation can reduce excess rural labour supply and land fragmentation, two factors that have been linked to low land productivity (Desiere and Jolliffe, 2018_[4]). Lastly, increasing demand for food from growing urban populations can increase rural income levels.

Countries benefit most from the shift from low-productivity agriculture to high-productivity manufacturing and services at the height of the urbanisation process, when migration from rural to urban areas is at its peak. Africa needs to exploit the urban productivity advantage now, by investing in better planned cities with more efficient infrastructure (Venables, 2018_[5]). The cost of poor planning and investment in cities in terms

of lost productivity gains is arguably highest in developing economies, because it holds back the emergence of a productive manufacturing sector. African cities’ fragmentation and poor connectivity limit access to jobs, leading to labour misallocation and reducing productivity (World Bank, 2020_[6]).

National economic policies have a strong spatial impact, which needs to be anticipated

National economic policies and sector initiatives have a strong and often durable spatial impact, and space-blind² policies can be costly. A spatial development lens takes into account the national system of cities, the distribution of people and activities in a territory, and their roles in socioeconomic development. Urban development is path-dependent. Many African cities were established in the colonial period to facilitate the production and export of natural resources and agricultural commodities. The cities persisted and grew, even as the extractive economic activities and the transport systems that sustained them, such as railway lines, diminished in importance. To some extent, the infrastructure stock these cities inherited

at independence and the migration and growth inertia that continued in the subsequent periods have sustained them, even after they lost their original economic advantages (Jedwab and Moradi, 2016_[7]).

The lesson is clear: economic policies have robust and enduring spatial impacts. Industrial policy is another prime example. Historically, industrial policies in developing economies have promoted import substitution and exports. Where high technology industries requiring highly skilled workers became the focus, growth has tended to be concentrated in a few large urban centres, especially in coastal locations, as has been the case in countries like Korea (Fullerton, 1997_[8]). In Africa, the state-led drive for import substitution industrialisation of the early post-colonial period coincided with rapid urban population growth, particularly in the largest cities, where industrial job opportunities were concentrated. Few alternative locations for industrial growth outside the capital or primary cities existed, as infrastructure and human resource capacity remained limited.

Policies in sectors that can appear to be further removed from cities, such as agriculture and food production, can have a potent effect on cities, underscoring the need for a spatial lens in development. Interventions to increase agricultural productivity, for example, could lead to the emergence of dynamic small and intermediary cities that capitalise on domestic food value chains in the targeted agriculture belt. The relationships between economic policies and spatial outcomes, however, are not always linear. Their intended and unintended consequences need to be carefully assessed and managed.

Urban investment across sectors varies in scale, is sporadic and should be co-ordinated

The economic case for investing in African cities is compelling. Africa’s urban population is poised to nearly double over the next two decades,³ and by 2025, African cities will already account for nearly two-thirds of GDP and an even greater share of GDP growth (MGI, 2011_[9]). “Poor infrastructure shaves up to 2 % off Africa’s average per capita growth rates” and severely affects “firms with high value addition, broad job opportunities, and wide sectoral linkages” (AfDB, 2018, p. 73_[10]). Although, compared to other regions, Africa would benefit most from infrastructure improvements, African cities remain under-planned and underinvested. Poor infrastructure is reflected, for example, in the high cost of electricity, which reduces firms’ competitiveness. On average, African firms pay

between USD 0.07 and USD 0.10 more per Kilowatt hour for electricity than firms in East Asia and South Asia. Estimates of the annual total African infrastructure investment gap range between USD 67.6 billion and USD 107.5 billion, figures that will increase with increasing levels of urbanisation. Strategic infrastructure such as ports, highways, digital communications backbones and Special Economic Zones (SEZ) are national in their geographic scope, but are fundamental to urban economies. Transport, energy and ICT, which account for 70% of national infrastructure investment, are critical to urban economic performance (UNECA, 2018b_[11]).

While investment in cities is important, not all investment has an equal impact. To maximise the benefits of investment, investments need to be well planned and co-ordinated. Capital investment in cities, such as housing, commercial properties, industrial plants and infrastructure, has a long life and is immobile. The value of each element depends on other investments in the urban area. Each investor, including households, entrepreneurs and public authorities, needs to know what other investors are going to do in order to make good investment decisions (Collier, 2017, p. 14_[2]). Moreover, the effectiveness of public investments by different levels of governments depend on each other. For example, investments in a SEZ undertaken by a Ministry of Commerce might depend on parallel investments in road infrastructure linking the SEZ to a port, which might be the responsibility of the Ministry of Transport.

Horizontal and vertical co-ordination between firms, between economic sectors, and between levels of government is key to maximising the complementarities between investment decisions. Co-ordination is also essential within individual urban sectors such as housing, due to the multi-dimensionality of inputs, such as land, finance and skills, and the multiplier effect that urban investment generates in terms of jobs, livelihoods, income and property taxes. According to one estimate, making long-term mortgages available, for the value of 80% of the cheapest house, could potentially create 1.3 million construction jobs in Africa (CAHF, 2017_[12]), significantly increasing tax revenue. Often, however, public spending on investments comes from budgets other than the budgets to which revenues from the investments will be allocated. Without proper co-ordination between sectors, profitable public investments may not be made, because decision makers factor in only the costs for one budget, without taking into account the revenues that will accrue to another budget.

Key considerations for national policy making on cities' economic role

The empirical analysis presented in Chapter 1 of this report demonstrated that African cities are productive, and that labour productivity is estimated to increase on average by 0.3% if the urban population increases by 10%. Cities also create benefits in a wide range of other important dimensions. At the same time, the potential of African cities is not fully realised, and major deficits in housing, infrastructure and decent work persist. This section discusses policy issues for maximising the economic role of cities, to be considered at the national policy level.

Urbanisation and economic growth are closely related across several dimensions, but the relationship

between the two is complex and non-linear. Not all cities have similar levels of economic performance, and the measures needed to encourage economic development can vary from city to city. A host of factors contributes to urban productivity and helps to determine whether cities will reach their productive potential. The types of interventions and investments a city most urgently needs depend on its context, opportunities and the specific deficits it faces. The empirical literature on which factors determine the productivity of African cities is both extensive and preliminary, especially considering the complexity of factors at play and the difficulty of measuring their impacts accurately. Still, it is possible to say with relative certainty that some factors significantly affect the ability of African cities to achieve their productive potential.

Box 3.1. The literature on economic development in cities

Despite the extensive literature on the productivity of cities, studies on African cities and on cities in developing countries in general are limited. The table below presents a comprehensive overview of the literature on determinants of economic development in cities in developing countries, and forms the basis of the discussion in this section.

The table includes reports from international organisations such as the African Development Bank (AfDB), the International Monetary Fund, the OECD, the United Nations Development Programme (UNDP), the United Nations Economic Commission for Africa (UNECA),

the United Nations Human Settlements Programme (UN-Habitat) and the World Bank, and think tanks such as the Brookings Institution and the International Growth Centre. It also includes empirical studies that measure the impact of various factors on urban economic performance (measured by firm productivity, wages, GDP, employment or structural transformation) specific to cities or to sectors that are typically urban, such as manufacturing. Creating an exhaustive list of these studies was not feasible, so the emphasis is on relatively recent studies.





Table 3.1. Literature on factors contributing to the economic performance of developing world cities

Factor contributing to urban economic performance ¹	Literature related to cities in the developing world
Human capital	Asmal et al. (2020 _[13]); Barro (2001 _[14]); Calderón & Servén (2010a _[15]) (2010b _[16]); Calderón, Moral-Benito & Servén (2011 _[17]); Chauvin et al. (2017 _[18]); Chen & Dahlman (2004 _[19]); Commission on Growth and Development, (2008 _[20]); Dinh, et al. (2012 _[21]); Dollar, Hallward-Driemeier & Mengiste, (2005 _[22]); Hasan et al. (2017 _[23]); Isaksson, (2007 _[24]); Kim & Loayza, (2019 _[25]); Lall, Henderson & Venables, (2017 _[26]); Newman et al., (2016 _[27]); Page et al., (2020 _[28]); Quintero & Roberts, (2018 _[29]); UN-Habitat, (2020 _[30]); Wei & Hao, (2011 _[31]); World Bank, (2004 _[32]); World Bank, (2009 _[33]); York & Fraser (1989 _[34]),
National infrastructure	AfDB, OECD & UNDP, (2016 _[35]); Amirtahmasebi, (2016 _[36]); Andres, Biller & Dappe (2015 _[37]); Asmal, et al. (2020 _[13]); Boopen (2006 _[38]); Calderón & Servén (2010a _[15]); Calderón & Servén (2010b _[16]); Calderón, Moral-Benito & Servén (2011 _[17]); Chen & Dahlman (2004 _[19]); Collier (2016 _[39]); Combes & Gobillon (2015 _[40]); Commission on Growth and Development (2008 _[20]); Escribano, Guasch, & Pena (2010 _[41]); Hulten (1996 _[42]); Isaksson (2007 _[24]); Lipscomb, Mobarak & Barham (2013 _[43]); McCulloch & Zileviuciute (2017 _[44]); Newman et al. (2016 _[27]); Njoh, (2009 _[45]); Page, et al. (2020 _[28]); Paunov & Rollo (2015 _[46]); Quintero & Roberts (2018 _[29]); Seethepalli, Bramati & Veredas (2008 _[47]); World Bank (2004 _[32]); World Bank (2009 _[33]); World Bank (2013 _[48]); York & Fraser (1989 _[34])
Urban infrastructure	AfDB, OECD & UNDP (2016 _[35]); Arnold, Mattoo & Narciso (2006 _[49]); Aterido & Hallward-Driemeier (2007 _[50]); Aterido, Hallward-Driemeier & Pagés (2007 _[51]); Asmal, et al. (2020 _[13]); Bacon & Kojima (2016 _[52]); Bastos & Nasir (2004 _[53]); Collier (2016 _[39]); Commission on Growth and Development (2008 _[20]); Dethier, Hirn & Straub (2010 _[54]); Dollar, Hallward-Driemeier & Mengiste (2005 _[22]); Escribano & Guasch (2005 _[55]); Escribano, Guasch, & Pena (2010 _[41]); Hasan et. al. (2017 _[23]); Hommann & Lall; limi (2011 _[56]); Kriticos & Henderson (2019 _[57]); Lall, Henderson & Venables (2017 _[26]); Mensah (2018 _[58]); Metropolis (2019 _[59]); Page, et al. (2020 _[28]); Peters, Vance & Harsdorff (2010 _[60]); Rijkers, Söderbom & Loening (2010 _[61]); UNECA (2018 _[62]); World Bank (2009 _[33]); World Bank (2013 _[48])
Regulatory environment	Acemoglu, Johnson & Robinson (2001 _[63]); Bastos & Nasir (2004 _[53]); Commission on Growth and Development (2008 _[20]); Dethier, Hirn & Straub (2010 _[54]); Hallward-Driemeier, Wallsten & Xu (2006 _[64]); Isaksson (2007 _[24]); Kriticos & Henderson (2019 _[57]); McMillan & Rodrik (2011 _[65]); McMillan, Rodrik & Verduzco-Gallo (2014 _[66]); Newman et al. (2016 _[27]); Page et al. (2020 _[28]); Rodrik, Subramanian & Trebbi (2004 _[67]); World Bank (2004 _[32])
Corruption	Aterido, Hallward-Driemeier & Pagés (2007 _[51]); Bastos & Nasir (2004 _[53]); Commission on Growth and Development (2008 _[20]); Dethier, Hirn & Straub (2010 _[54]); Escribano & Guasch (2005 _[55]); Fisman & Svensson (2007 _[68]); Hallward-Driemeier, Wallsten & Xu (2006 _[64]); Newman et al. (2016 _[27]); World Bank (2004 _[32])
Finance	Aterido & Hallward-Driemeier (2007 _[50]); Aterido, Hallward-Driemeier & Pagés (2007 _[51]); Commission on Growth and Development (2008 _[20]); Dethier, Hirn & Straub (2010 _[54]); Dinh, et al. (2012 _[21]); Dinh, Mavridis & Nguyen (2012 _[69]); Dollar, Hallward-Driemeier & Mengistae (2005 _[22]); Rijkers, Söderbom & Loening (2010 _[61]); Page, et al. (2020 _[28]); World Bank (2004 _[32])
Economic sector composition	Abdel-Rahman & Fujita, (1990 _[70]); AfDB, OECD & UNDP, (2016 _[35]); Asmal, et al., (2020 _[13]); Commission on Growth and Development, (2008 _[20]); Gollin, Jedwab & Vollrath, (2016 _[71]); Henderson & Kriticos, (2018 _[72]); Isaksson, (2007 _[24]); Kriticos & Henderson, (2019 _[57]); McMillan & Rodrik, (2011 _[65]); McMillan, Rodrik & Verduzco-Gallo, (2014 _[66]); Page, et al., (2020 _[28]); UN-Habitat, (2010 _[73]); UN-Habitat, (2020 _[30]); York & Fraser, (1989 _[34])

1 Public finance is not listed here, although it is very frequently mentioned as a precondition to economically successful cities in reports on the topic. Finance, which is covered in Chapter 5, operates by enabling the other factors. Good governance is similarly mentioned in many reports and enables the other factors.

Cities become more productive as they increase in size, but also face major constraints

Agglomeration economies make larger cities more productive than smaller cities. This pattern exists globally and can also be found in Africa. However, part of the urban productivity advantage is lost in Africa, due to the higher costs of operating in cities. African cities are more expensive than those in countries with similar income levels, by a margin of up to 31% (Nakamura et al., 2016_[74]). Industrial labour is more costly than in countries at comparable income levels in other regions, with few countries appearing to have a low labour cost advantage to support competitiveness in manufacturing (Gelb et al., 2020_[75]). Because of lack of capital investment in the face of rapid population growth in urban areas, many African cities experience fragmented urban development, housing problems and lack of efficient and affordable transport systems, reducing accessibility of workers to jobs, for instance. For example, in Nairobi, passengers on Matatu (privately owned minibuses) can access only 4 % of jobs on average within 30 minutes, 10% within 45 minutes, and 20 % within 60 minutes. In Ugandan cities, 70 % of commutes are on foot, often for long distances (Grover, Lall and Timmis, 2021_[76]).

The increase in urban costs is an inherent part of agglomeration economies. As a city grows, depending on the type and characteristics of economic activities and prevailing technology in production and connectivity, it reaches a point where costs and disamenities begin to outweigh the benefits of increasing size. However, in Africa, many cities appear to be arriving prematurely at this point. This is because they grow without commensurate investment in infrastructure and housing, and often with inadequate planning. Most primary cities in Africa are not large by global standards, but because of the speed and scale of urbanisation in the context of low-income levels and lagging infrastructure, continued urban growth increases urban costs and congestion that need to be mitigated (Henderson and Kriticos, 2018_[72]).

Given the manifold benefits of urbanisation that are documented in Chapter 1 of this report, policies that aim to reduce urban population growth would be an economically and socially harmful solution to high urban costs. Instead, more and more effective investments are needed. Urban development has often preceded planning, leading to settlements without connected street networks and weak public services. Land use is often inefficient and socially segregated, with valuable central locations only sparsely developed,

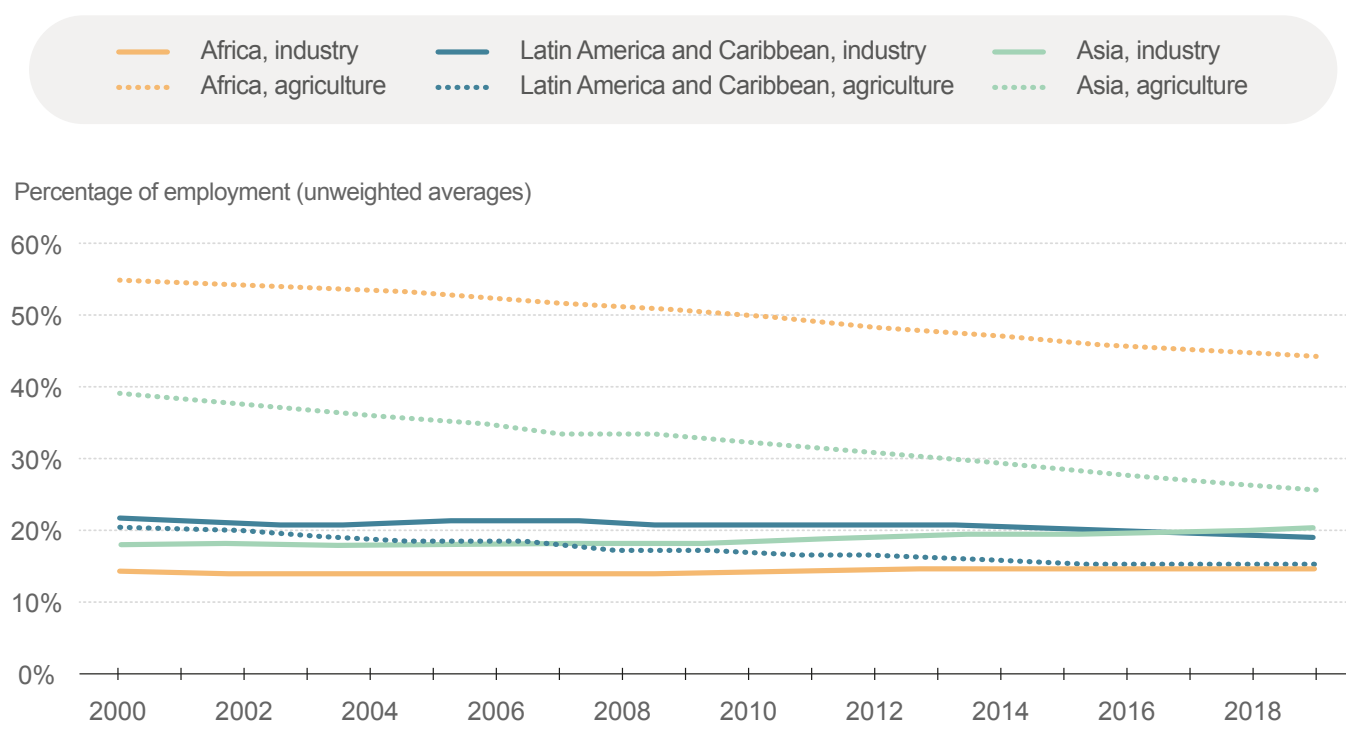
while densely populated areas such as slums are underserved by infrastructure. Potential efficiency gains of density are not exploited due to poor land use planning, weak land administration and rigid zoning rules. The result is increasing urban inefficiency, reflected in unsustainable rises in living costs, including high commuting costs, excessively high housing-to-income ratios, high costs of doing business, and growing unemployment (UNECA, 2017_[77]). These urban costs and disamenities diminish the net gains of agglomeration economies and urban density, and potentially deter firms and educated workers from moving to larger cities (Grover, Lall and Timmis, 2021_[76]).

The economic power of cities hinges on the jobs they create

Workers in African cities are more likely to be employed in skilled occupations and are less at risk of underemployment than their rural counterparts. However, more than half of employed men and more than three-quarters of employed women are in unskilled occupations (Chapter 1). A large informal sector and unemployment are further major concerns. Creating more decent jobs is an overriding policy requisite for African cities.⁴ Chapter 1 showed that the sector composition of urban jobs has remained largely stable throughout the last two decades. Despite some positive recent shifts, overall structural change due to urbanisation has frequently not increased growth as much as it might have, because most of the workers who moved out of agriculture have ended up in low-productivity service activities, mainly in the informal economy (McMillan, Rodrik and Verduzco-Gallo, 2014_[66]).

In other regions, manufacturing has been a key element of productive urban job creation, but African cities have seen mixed results in the sector. The share of formal manufacturing jobs in total global value chains is as low as 10% in Ethiopia and Senegal, or as high as 20% in South Africa, compared to more than 35% observed in benchmark countries such as Bangladesh, Brazil, China, India and Malaysia (World Bank, 2020_[6]). Employment in manufacturing has grown slightly in recent years (Figure 3.2). This is significant given the prior stagnation of manufacturing employment share at 7.2% between 1990 and 2010, and the relative decline observed in Latin America and the Caribbean during the same period. “Although the level of manufacturing activities is low in comparison to other regions, this increase in manufacturing employment in Africa is an important reversal to a long-run de-industrialisation trend that was documented for the period from 1960 to 2011” (Kruse et al., 2021, p. 8_[78]).

Figure 3.2. Employment shares in industry and agriculture by region, 2000-19



Note Percentage of employment. Unweighted average of countries.

Source Data: World Development Indicators (WDI); Chart by authors.

In the past, urban job creation has not always been a priority. A central issue for national economic policy is to set priorities for public investment. This involves marshalling scarce resources in support of strategic economic sectors with the potential to drive growth and the creation of decent jobs. In African national development planning, cities have not always featured prominently among the locations of targeted economic sectors, leaving decent urban jobs as a critical national policy gap (UNECA, 2017b_[79]). Policies targeting economic sectors that can generate large numbers of productive jobs will be central to achieving urban economic potential and national economic structural transformation.

The recent move to adopt a new generation of industrial policies is a promising move toward a potential renaissance of manufacturing jobs in many African countries. Even if they are successful, manufacturing firms, particularly those engaged in export trade, may not necessarily be employment intensive. A bifurcation emerged during the 2010s, when Africa appears to have recovered some ground. Countries classified as manufacturing exporters increased their output of manufactured products, but the share of

employment in manufacturing declined, whereas non-manufacturing exporters increased employment, but not productivity. In the case of industrialisation in non-manufactures exporters, domestic demand, which has increased due to increase in agricultural income, public expenditures and external transfers, are likely to have expanded the market for (lower-quality) manufactured goods (Diao et al., 2021_[80]).

While a strong manufacturing sector is important for the economic development of Africa, it is not sufficient. Modern, tradable services, which tend to cluster in urban areas, such as ICT-based services, tourism, transport and logistics, as well as agro-industrial production,⁵ are in general high-productivity sectors with potential for boosting productivity and urban jobs (Newfarmer, Page and Tarp, 2019_[81]). These sectors are especially important, because it is unclear to what degree African countries can pursue the development strategies of East and Southeast Asian countries that are heavily dependent on labour-intensive manufacturing. Since East and Southeast Asian countries still have strong comparative advantages in these sectors, it is difficult for other countries to replicate these strategies.

Employment in manufacturing in African cities has been driven by small firms. However, while small firms absorb labour, their productivity has not increased. Conversely, the employment share of larger, registered firms is declining, while their output share is rising. This observation aligns with those of Diao et al. (2021_[80]), who observed that in Ethiopia and Tanzania, large firms have experienced productivity growth without an increase in employment, while smaller firms have absorbed workers without an increase in productivity. Related to this are apparent challenges in increasing firm size: micro- (fewer than 20 employees) and small enterprises (21 to 50 employees) rarely graduate to becoming medium (51 to 100) and large-size firms (<101). In Ethiopia, for example, 97% of formal jobs in manufacturing are created by medium and large firms (Mukim, 2016_[82]), and according to one study, just 7% of those firms with between 10 and 30 workers employed more than 50 workers after ten years, suggesting high mortality and stubbornly low average sizes of small businesses (Shiferaw and Bedi, 2013_[83]). Small firms benefit from locating in cities for all the reasons large firms do, including a large, concentrated customer base, access to products and services, and access to labour.

Cities can take steps to support the scaling up of firms, including improving the overall business climate and removing barriers such as access to finance and technology to small and micro enterprises (Bartik and Sotherland, 2019_[84]). Formalising land markets can help small firms find urban locations to expand production. Similarly, productivity of micro- and small enterprises can be boosted with simplified regulatory processes, expanding access to finance to firms in the formal and informal sectors, and enhancing access to skills and capacity development, including lifelong learning for managerial as well as workforce levels.

Human capital contributes significantly to urban productivity

There is strong empirical evidence that human capital, especially education and skills, plays a role in urban economic performance, and the literature on African cities generally supports the conclusion that human capital matters (Table 3.1). Various studies suggest that human capital is even more important than infrastructure and other critical factors. In a study of 115 developing countries, Kim and Loayza (2019_[25]) find that improvements

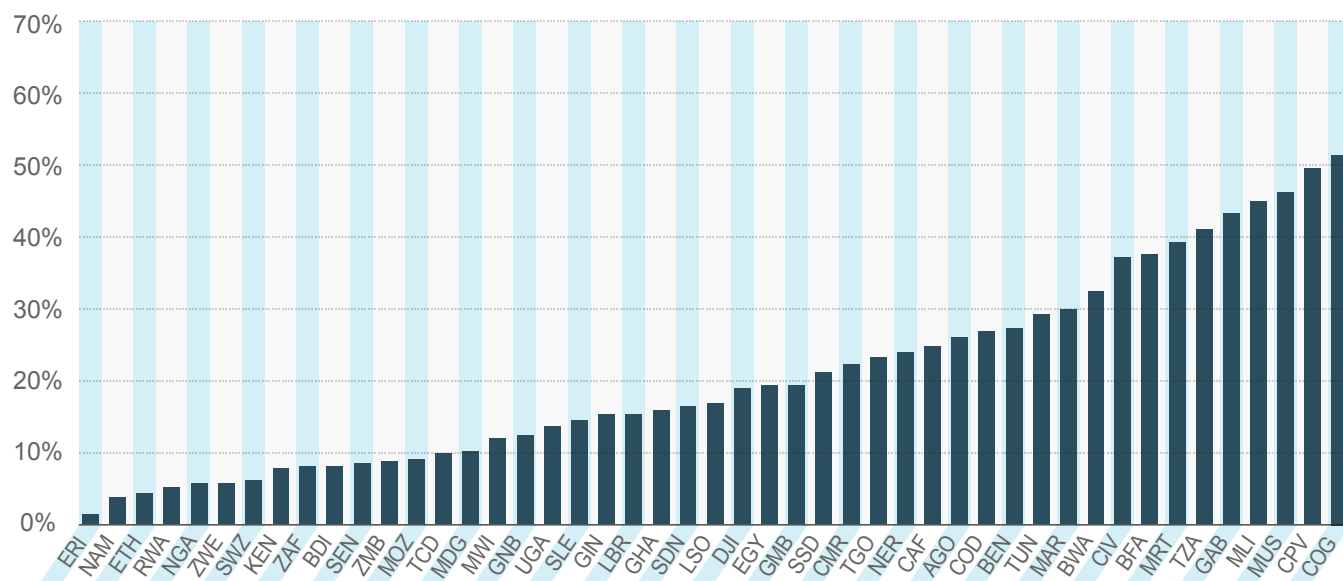
in education were by far the biggest contributor to total factor productivity growth (accounting for nearly half) in the two decades between 1994 and 2014, above innovation, market efficiency, infrastructure and institutions. In a study of 88 countries, including 30 in Africa, Calderón, Moral-Benito and Servén (2011_[17]) find that human capital is more powerful than infrastructure in predicting GDP per worker. Quintero and Roberts (2018_[29]) find in a study of 16 Latin American and Caribbean countries that human capital outweighs the impact of density and connectivity to other urban markets in determining urban wages.

Data from Chapter 1 shows that levels of education are higher in cities than in rural areas, and that they rise as cities increase in size. Workers in large cities have more opportunities to learn new skills and accumulate work experience, the value of which persists into the future, including if they relocate to other cities (La Roca and Puga, 2017_[85]). This has two policy implications: 1) investing in skills has considerable individual and societal returns; and 2) barriers to urban growth and thus accumulation of human capital, such as housing supply or provision of urban services, should be removed (Glaeser and Xiong, 2017_[86]).

Skills amplify agglomeration economies, and agglomeration economies incentivise skill accumulation, because they lead to higher wages for skilled workers in cities (Glaeser and Resseger, 2010_[87]; La Roca and Puga, 2017_[85]). Empirical studies show that skilled workers, with good soft skills and experience, benefit most from being in large cities by earning higher wages (Bacolod, Blum and Strange, 2009_[88]; Kriticos and Henderson, 2019_[57]). Consequently, workers migrating from rural to urban areas invest in skills, because the impact of skills on workers' wages is higher in urban than rural areas.

In Africa, education levels in cities have been raised significantly in the past three decades. The number of years of schooling of people aged 18-29 in cities with more than 1 million inhabitants rose from an average of 6.5 years to more than 9 years between the 1990s and the 2010s (see Chapter 1). This is likely to have a lasting positive impact in the coming decades, given the economic and social benefits of a better education throughout a person's lifetime. Further efforts are needed, however, to increase the number of skilled workers. As shown in Figure 3.3, the shortage of skilled workers is still cited as a major constraint for firms in many African countries.

Figure 3.3. Percentage of firms identifying inadequate workforce skills as a major constraint by African country



Source (World Bank_[89]), most recent year available by country; chart by authors.

Increasing the number of skilled workers will also benefit less educated workers, including those in the informal economy. The tasks of skilled and unskilled workers are complementary. Larger numbers of skilled workers tends to improve the employment prospects and wages of unskilled workers (Eeckhout, Pinheiro and Schmidheiny, 2014_[89]). Less educated workers benefit from this complementarity in various ways. They learn from their interaction with educated workers and become more productive; educated workers innovate and create new jobs that also benefit less educated workers. Meanwhile, educated workers earning higher incomes purchase more locally produced consumer goods and services, which creates jobs for less educated workers; and lastly, a reduction in the number of low-skilled workers pushes up the wages of those with lower skills (Winter, 2020_[90]).

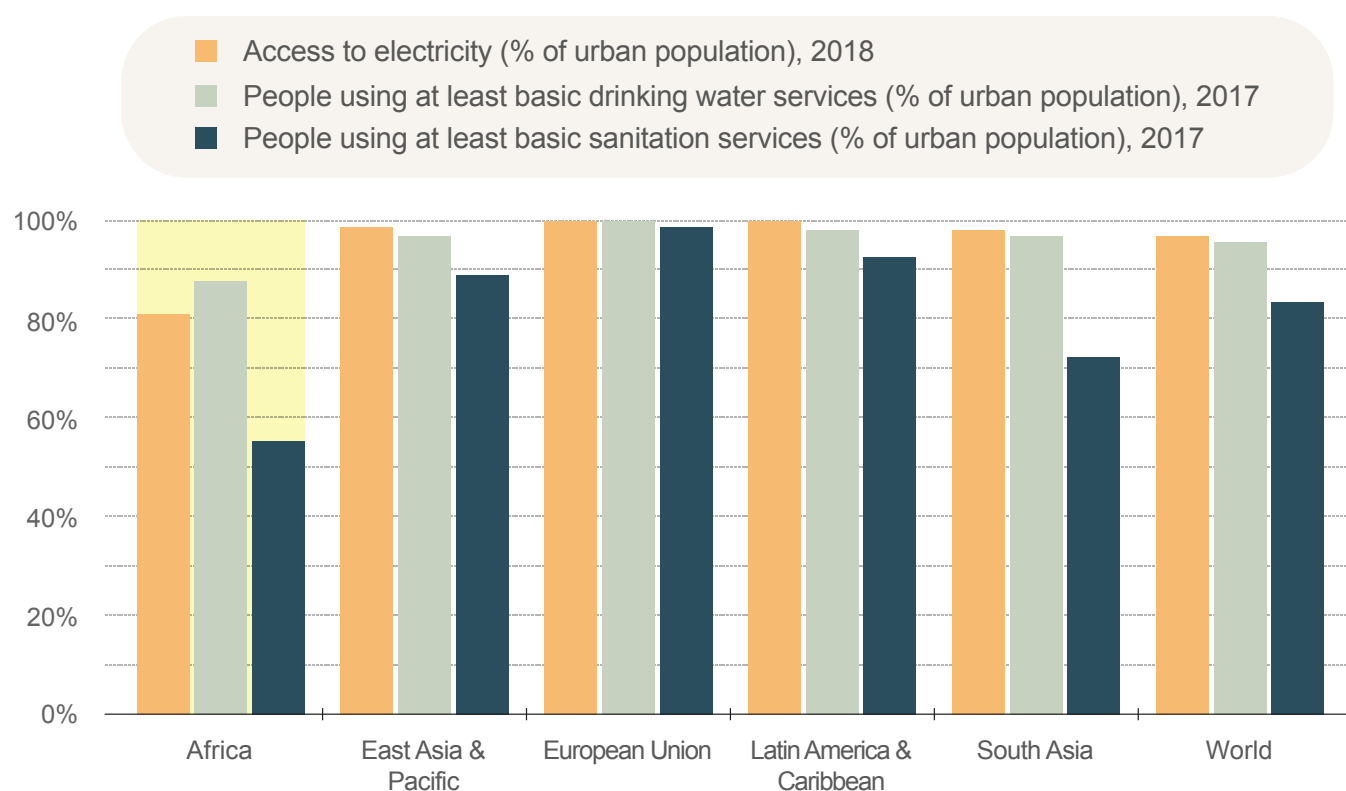
Infrastructure is critical for urban development

The benefits of urbanisation depend strongly on supporting infrastructure and institutions (Turok and McGranahan, 2013_[91]).⁶ While the data in Chapter 1 has shown that African cities generally provide better

access to infrastructure than rural areas, and larger cities generally do better than smaller cities, many African cities still lag behind other regions in basic urban services (Figure 3.4).

Urban infrastructure, above all other factors except human capital, has the clearest support in the literature for its role in the productivity of developing cities. In the African context, the need for reliable electricity has been most thoroughly documented (Straub, 2008_[92]). In a study of 26 African countries, Escribano, Guasch and Pena (2010_[41]) find that electricity is the most important factor in firms' total factor productivity. While the importance of electricity access is well documented, it is often difficult to distinguish the effects of different dimensions from each other because the quality of various dimensions of infrastructure is closely correlated. Moreover, the most pressing infrastructure needs vary from city to city, and as electricity grid connections become more widespread, especially in large cities, where approximately 80% of households have access to electricity (Figure 3.4), closing gaps in access to other types of infrastructure in sectors including water, sanitation, transport and ICT will become increasingly important.

Figure 3.4. Urban access to electricity, water and sanitation by region



Source (World Bank_[94]) World Development Indicators (WDI) ; chart by authors.

Many studies emphasise the importance of urban transport, which is fundamental for the connectivity of workers and firms and hence the generation of agglomeration economies (AfDB/OECD/UNDP, 2016_[35]; Kriticos and Henderson, 2019_[57]; Lall, Henderson and Venables, 2017_[26]; Page et al., 2020_[28]; World Bank, 2013_[48]). Some reports discuss the role of mass transit in particular (Collier, 2016_[39]; World Bank, 2013_[48]; UN-Habitat, 2020_[30]). While the theoretical case for the importance of transport is clear, empirical work on the role of intra-urban transport is less common. Nevertheless, the existing empirical data generally show the important effect of various elements of (public) transport infrastructure.

Infrastructure at the national level is also important, and not solely within cities.⁷ This is particularly true for transport infrastructure, as productive cities must be able to connect to external markets (see Chapter 2). Other elements of national infrastructure, such as power generation and telecom backbone infrastructure, are also fundamental as a pre-condition for good intra-urban infrastructure. Infrastructure provision is

another policy field where national and local responsibilities overlap and need to be co-ordinated.

Institutions and the regulatory environment affect urban productivity

The regulatory environment is widely recognised as important for urban productivity; but there is no consensus on which regulations matter most and in what contexts. Various studies focus on different elements of the regulatory environment, including labour market regulations, regulations to encourage competition between firms, protection of property rights (not specific to land rights, which are discussed below), and the ease of doing business in general. Corruption seems to be a significant constraint on urban economic performance in developing countries, although less so in Africa than in other regions (see sources in Table 3.1).

Regulations governing the ease of trade and logistics have also been found empirically to be a major factor in the performance of urban firms (Dinh et al., 2012_[21]; Aterido and Hallward-Driemeier, 2007_[50]; Dollar,

Hallward-Driemeier and Mengistae, 2005_[22]; Escribano, Guasch and Pena, 2010_[41]). This is not surprising, given that a common economic challenge among African cities is the prevalence of non-tradable sectors and the difficulty of creating jobs in more productive tradable activities, as well as the dependence on imports for many inputs to urban production. Addressing barriers to trade do not typically feature in the lists of top policy recommendations in major reports on African cities, an area that could potentially be strengthened in the development discourse on the topic.

Lastly, the ability of firms to access finance, which is closely linked to the institutional environment, is one factor whose importance in urban economic performance is clearly supported by the evidence (Table 3.1). Difficulties in accessing finance are especially constraining for small firms (Aterido, Hallward-Driemeier and Pagés, 2007_[51]) and are also a major constraint for many local governments (see Chapter 5). Thus, they hinder the upscaling of firms and prevent local governments from investing in infrastructure.

Urban form is important for the functioning of cities, but empirical evidence on the topic is limited

The benefits of cities arise from proximity and connectivity of economic actors. It is thus no surprise that urban form and urban planning are widely discussed in the development discourse as major determinants of the economic performance of African cities. Fragmented urban areas with large differences in population densities, long commuting distances within cities and a lack of good intra-urban transport prevent the emergence of agglomeration economies and reduce economic growth (Collier, 2016_[39]; Lall, Henderson and Venables, 2017_[26]; UN-Habitat, 2020_[30]). Similarly, urban planners have long argued that many aspects of urban

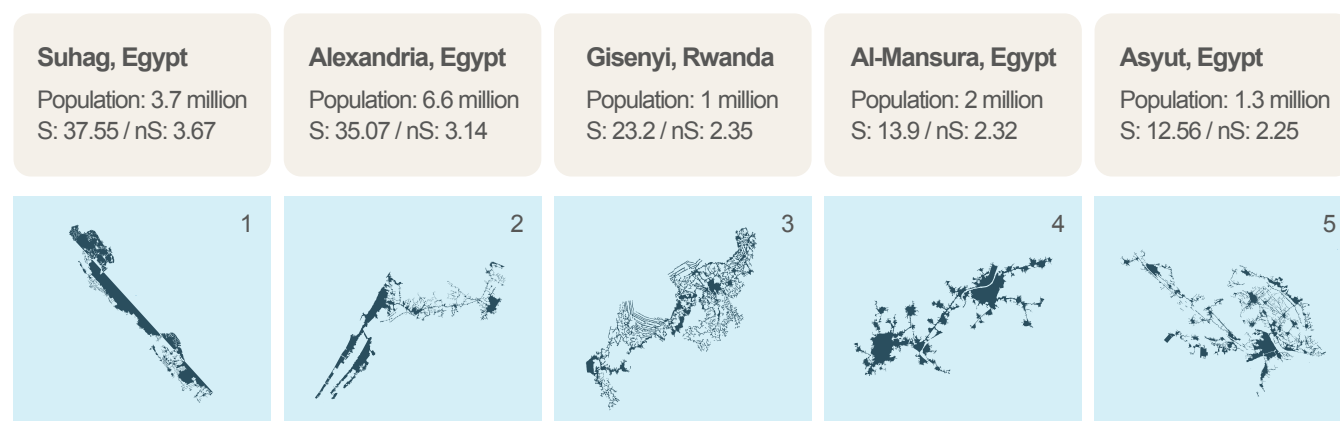
form have important consequences for the functioning of cities, including the shape, size and density of cities, their urban block layout and road grid, land use, and building types and design (Dempsey et al., 2008_[93]). These aspects influence many determinants of urban productivity, including how people interact with each other, whether roads can transport a large number of users efficiently or are prone to congestion, and how costly it is to service the city with infrastructure.

While the impact of various dimensions of urban form receives more and more attention from researchers and policy makers, many of them cannot yet be measured systematically. Robust empirical evidence on the impact of most dimensions of urban form is scarce, in particular in developing country contexts. An exception is Harari (2020_[94]), who finds that Indian cities with more compact urban shapes have higher levels of population growth and perform better in terms of accessibility and quality of life. The Africapolis database (OECD/SWAC, 2018_[1]) contains data on the footprint of African cities as of 2015 and can be used to study the shape of cities using a methodology similar to that of Angel, Parent and Civico (2010_[95]) and Harari (2020_[94]). The average distance between any two points within the city is computed and normalised by the total area of the city,⁸ so that it does not simply reflect city size. The more compact a city is, the shorter the average distance between two points within it. Figure 3.5 shows the footprint of the five African cities of over 1 million inhabitants with the longest average distance between two points and the five cities with the shortest average distance, respectively. Two patterns are notable. Cities with long distances do not form a round shape and have a discontinuous urban fabric, with many gaps between built-up areas. In contrast, cities with short average distances between points are rounder and have few gaps between built-up areas.

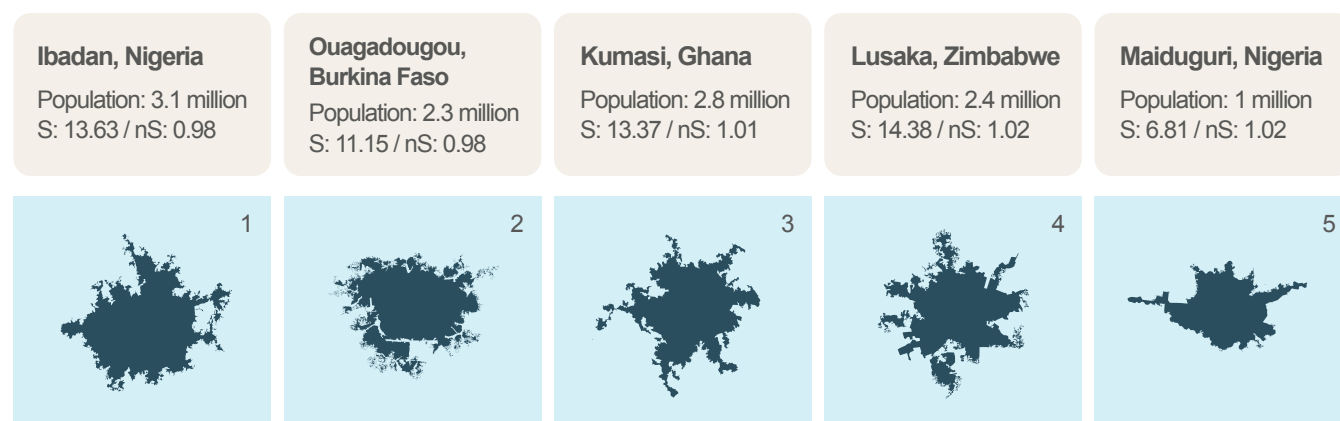
Figure 3.5. Urban form and its effect on population density

Large African cities with the longest (top row) and shortest (bottom row) average distance between any two points within the city

Biggest nS



Lowest nS



Note The top row shows the shape of the five African cities above 1 million inhabitants with the longest average distance between two points within their territory (adjusted for their area). The bottom row shows the shape of the five African cities of more than one million inhabitants, with the shortest average distance between two points within their territory (adjusted for their area). The urban footprint of all African cities can be downloaded on africapolis.org.

Note that S is a disconnected index that shows the average distance between pairs of random points within the city. nS is a normalized disconnected index defined as S divided by radius of the equivalent area circle, i.e. the radius of a circle that has the same area as the built-up area. The larger the value of nS, the more disconnected is the urban footprint of the city.

Source OECD/SWAC calculations based on (OECD/SWAC, 2018_[11]), following Angel, Parent and Civico (2010_[95]) and Harari (2020_[94]).

Beyond compactness, many other dimensions of urban form have an impact on productivity and the functioning of cities. Transport-oriented development (TOD) is an important instrument for improving accessibility and reducing congestion, involving the construction of housing and commercial developments primarily along transport corridors. Where local governments do not have the capacity to implement transport-oriented development, preventing the unplanned development on land that will be needed for future transport corridors is an important short-term measure to reduce the future costs of infrastructure construction (Angel, 2011_[96]).

Other important measures to create productive and liveable urban forms include creating well-served dense neighbourhoods in central locations. Density encourages interactions that create the innovations from which agglomeration economies arise. Dense neighbourhoods, however, need good infrastructure to function efficiently and provide liveable environments. It is possible to create highly productive and desirable neighbourhoods with densities of more than 50 000 inhabitants per square kilometre with the right planning policies and investment (e.g. providing effective public transport and constructing high-quality public spaces). However, similar densities in

a poorly serviced slum limit productivity and result in poor living conditions.

Likewise, it is important to create business districts and industrial areas that allow firms to locate close to customers, suppliers and competitors. In many cases, excessive single-use zoning, over-zoning and restrictive-use segregation create more drawbacks than advantages, because they encourage sprawl, increase travel distances and reduce accessibility. Under restrictive land use regulations, even when plots are planned and available, development becomes fragmented, precluding opportunities for firm clustering and future expansion and reducing firm competitiveness.

Improving urban form is not easy and often demands trade-offs. For example, low-income and low-skilled households in Kampala concentrate on “Mailo land”, which has a customary tenure arrangement, because it is affordable and offers a dense social network. However, the tenure arrangement comes at the cost of economic efficiency. According to one estimate, converting all Mailo land in Kampala to leasehold would increase aggregate urban real incomes by 2% in the absence of localisation economies and 6.7% in their presence, particularly benefiting low-skilled workers. Income growth would occur because formalisation would make it possible to convert land to more productive uses. While the benefits from higher incomes would be significant, they could entail a loss of amenities to residents leaving the Mailo land, unless they were offered less expensive alternative housing solutions (Bernard, Bird and Venables, 2016_[97]).

Land markets are likely to have a major impact on urban productivity, but empirical evidence is scarce

Effective land markets are another precondition for effective land use. Land is by far the most valuable production factor in cities (OECD, 2017_[98]). Land markets are the main mechanisms for allocating land to its most productive uses, and their efficient functioning is a key factor for the economic development of cities. Without functioning land markets, misallocations of land to less productive uses will persist and will prevent the structural transformation of the economy, which is generally associated with massive changes in urban land use. For example, anecdotal evidence from Ethiopia suggests that “problems acquiring land often prevent firms ... with 4–5 employees from growing into businesses with more than 10–15 employees. To do so, they would need a larger workspace connected to affordable and reliable utilities and offering reliable transport links to markets for inputs and outputs. Most

small firms are located in the owner’s home or in small workshops” (Dinh et al., 2012, p. 67_[21]).

Land markets need to be well regulated because they typically have imperfections, such as large information asymmetries and potential monopolies. Informality prevents both the emergence of land markets and their effective regulation. Land titling and establishing up-to-date cadastres and land registries is a precondition for functioning land markets. Empirical evidence on the topic is mixed, however. Some preliminary evidence indicates that land tenure encourages productive economic activity (Bernard, Bird and Venables, 2016_[97]; Field, 2007_[99]) but other studies find no impact (Brasselle, Gaspard and Platteau, 2002_[100]; Galiani and Schargrodsky, 2010_[101]; Andreassen et al., 2020_[102]).

A quote from (Do and Iyer, 2008_[103]) rings true: “There is a certain amount of consensus among economists that better property rights institutions lead to improved economic outcomes. ... However, the empirical evidence on the importance of issuing formal titles to land is inconclusive, both on the overall effect of having property titles and on which dimensions of land rights are crucial,” (p. 531). The absence of good empirical evidence on the subject does not imply that it is unimportant; it is more likely that it shows the difficulty of measuring and quantifying the impact of land markets. Still, the lack of empirical evidence is a concern, given the high priority that the issue receives among experts (e.g. Lall, Henderson & Venables, (2017_[26]), and further studies on the topic are needed.

What matters most depends upon context-specific needs and complementarities

The issues discussed above include some of the most important factors determining the productivity of African cities. However, they do not exhaust the list of the issues policy makers need to address. The importance of various factors differs across cities, economic sectors and economic actors. For example, the performance of larger firms is more sensitive to access to electricity, corruption and the consistency of the regulatory environment, while small firms are affected more by access to finance and water outages (Aterido, Hallward-Driemeier and Pagés, 2007_[51]; Aterido and Hallward-Driemeier, 2007_[50]; Iimi, 2011_[56]).

Many of the issues discussed above are complementary, with the effectiveness of a given measure in one policy area being influenced by measures in other policy areas. For example, the effectiveness of new planning policies designed to increase the density of the built environment in central locations depends on

the functioning of land markets and on the capacity to provide infrastructure in the more densely developed areas. Complementary policy measures and investments that are aligned in space, timing and impact will

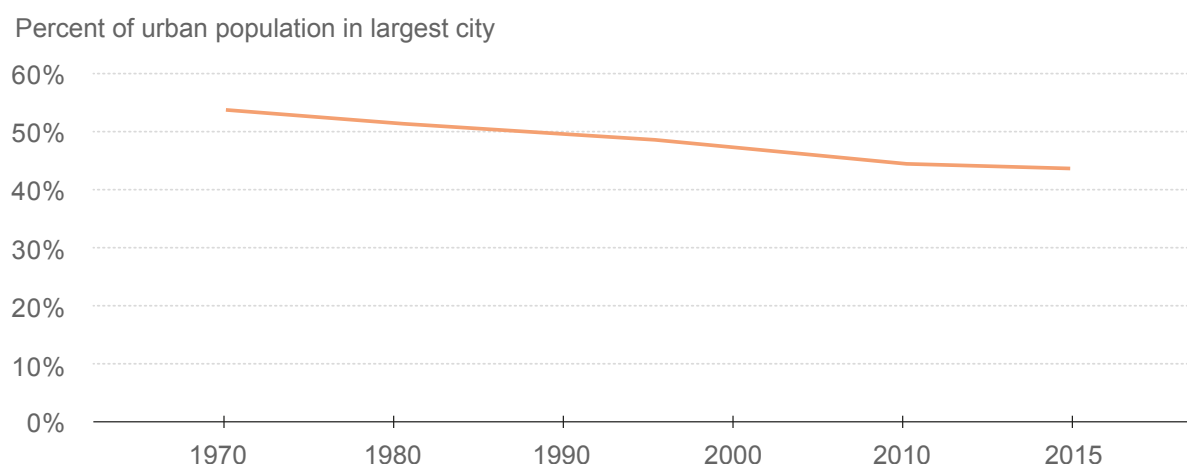
have synergies that are more powerful than isolated investments in one component or another. The factors examined here are interlinked, affecting each other and urban economic performance.

The system of cities drives production and influences regional inequalities

High urban primacy⁹ is often a concern for policy makers who want to shift urban population growth to other cities and boost productivity through systems of cities. While primacy in Africa has been high

historically, it has declined as income per capita and the number and size of secondary cities has increased. In 2015, the average share of the urban population living in the largest city in African countries was comparable to the global average and slightly lower than the average in Asia and Latin America.¹⁰

Figure 3.6. Unweighted average primacy across 54 African countries, 1970-2015



Source (OECD/SWAC, 2018_[11]), Africapolis (database); chart by authors.

Although primacy is no longer exceptionally high in Africa, it is still important to support a balanced urban development that allows cities of all sizes to reach their potential. Secondary cities in Africa have grown to a size typical in other parts of the world, but they do not necessarily have the same economic and administrative functions. Ideally, large cities provide the productive benefits associated with diversity, while small and midsize cities tend to provide localisation economies characterised by single-sector clustering and specialisation. Skill- and technology-intensive firms tend to cluster in large cities. By contrast, firms in mature industries or standardised product lines and activities, or firms in land and labour-intensive sectors, tend to benefit from localisation economies and cluster in small or midsize cities (Duranton, 2015_[104]; UNECA,

2018_[62]). Smaller cities can be important hubs for rural areas and contribute to their economic development (Chapter 1). They can also be the seat of government agencies and host universities and other higher education institutions, offering other possibilities for economic development.

While primary cities in Africa are the most productive, they also suffer from negative externalities. Low levels of investment in infrastructure and weak institutions for managing urban growth prevent them from reaping the full benefits of population concentration. This raises urban costs to both workers and firms and negatively impacts productivity. Neither neglecting primary cities nor delaying investment in intermediary cities is a solution. Both types of cities are needed, along with a mix of practical policy solutions

such as establishing Special Economic Zones (SEZ) (UNECA, 2017_[177]). Strategically selected intermediary cities should be promoted to relieve pressure from the primary city, to provide options for firms to locate and to facilitate factor mobility and churning between cities of different sizes, a fundamental pathway for dynamic productivity growth.

Many African countries have small populations and few large cities. Of 54 African countries, 14 have no cities with a population of between 300 000 and 1 million, and another 22 have only one city in that size range. Three policy priorities emerge: 1) improving the business environment in midsized cities; 2) increasing the economic role of small cities, in the context of the wider regional resource potential and economic linkages, including within agri-food system; and 3) overcoming economic fragmentation through economic and trade integration, to strengthen the roles of various cities in the larger regional urban system, especially between small countries where there are fewer prospects to diversify the national urban system. Policies affecting the functioning of labour markets, favouring the primary city, labour mobility and connectivity infrastructure will play a role (Duranton, 2015_[104]).

Population growth in small cities of under 50 000 requires scrutiny. Small cities account for nearly one-quarter of the region's urban population, and they should be given due attention in terms of their potential role in economic productivity. Their proximity to rural areas could make them instrumental in reducing rural poverty, particularly because in many countries, agriculture and associated activities are an important part of the economy (Henderson and Kriticos, 2018_[172]). As noted in Chapter 1, rural areas benefit from proximity to cities. In the context of urban networks and metropolitan areas, small cities could also benefit from the agglomeration economies of their larger neighbours, while avoiding rapidly growing urban costs (Camagni, Capello and Caragliu, 2016_[105]). This potential will depend on connectivity to the broader urban system and the density and intensity of economic linkages with the rural economies.

Integrating urbanisation into national economic planning: A policy framework

Countries' economic performance is determined by the economic performance of their cities. Establishing the fundamentals for economic growth in cities in terms of urban institutions, infrastructure and human capital

Regional connectivity is also critical for Africa's cities, given that borders can significantly limit trade (Chapter 2). Integration of regional trade is likely to boost urban production and benefit urban consumers. In an integrated regional system, cities are less constrained by their size or function. Already, regional urban clusters are emerging, and further regional integration policies can support city development in the broader regional urban system.

The dynamics of connectivity and agglomeration can increase inequality, another issue that can be managed through strategic national policies. Early in the formation of urban agglomerations, firms may locate in particular regions or localities, thanks to both natural and human-made advantages. These may include factors like basic infrastructure, sheltered harbours, natural resources and access to input and output markets. In time, these initial advantages result in a self-reinforcing process that leads to the emergence of strong industrial clusters or agglomerations, and regional disparities between areas with high industrial concentration and the rest of the country.

However, simple investment in infrastructure is unlikely to reverse the fortunes of lagging regions and attract firms, especially in sectors that are already well established in other leading regions (Deichmann et al., 2005_[106]; Schroeder, Lall and Schmidt, 2015_[107]). Standard manufacturing that is already concentrated in large agglomerations is unlikely to move to peripheral locations and smaller cities. One approach for alternate development strategies are improved rural-urban linkages. Strategies for promoting development in peripheral cities and regions include removing barriers to factor mobility, to allow outmigration of excess labour to places with more opportunities for job creation and poverty reduction. Other options include investing in the endogenous productive capacity of localities according to their competitive advantages and broadly investing in human capital and social services to raise the standard of living where productive job opportunities are scarce.

is necessary, but not sufficient, for sustainable growth. Important policy trade-offs need to be managed, and hard choices have to be made. Productive cities are part of a broader urban system, where cities sometimes complement each other and sometimes compete with each other. Likewise, trade-offs between productivity and employment have to be made. In theory,

high-productivity cities are also cities with high wages and high employment (Lobo, Bettencourt and West, 2011_[108]). In practice, the impact of productivity on wages and employment depends on the employment intensity of active sectors and their ability to stay competitive. This makes policy support for specific sectors or specific locations a strategic decision that involves a host of considerations, such as the balance between growth and spatial equity, the specialised profiles of cities, and the possibilities workers and firms have to move between cities.

Although urban productivity is a spatially bounded local phenomenon, its national implications cannot be overemphasised. Urban economic performance plays a growing role in determining national and regional development outcomes. Pairing national economic policy making with urban and spatial planning

processes is therefore critical. Public and private actors must co-ordinate scarce resources to support activities that drive growth and facilitate the process of economic structural transformation throughout the development process. Given the cost of inaction, rapid action is essential. Cities and urbanisation are integral to structural transformation and should be given due consideration in national economic planning. National Development Plans (NDPs) should acknowledge and support the economic role of cities and their linkages. UNECA (2018_[62]) proposes a framework in which four entry points are identified for bringing cities to the forefront of national economic planning: a) sector targeting, b) urban productivity, c) a system of cities and d) co-ordination and finance. A synopsis of this framework and the generic policy recommendations associated with it are presented below.

Figure 3.7. Four themes linking cities with national economic planning



Source (UNECA, 2018_[62]), An Urban Lens on National Development Planning in Africa: Guidebook for policymakers.

Table 3.2. Key thematic national policy questions for policy makers

Sector targeting for job-rich urbanisation	Urban productivity
<ul style="list-style-type: none"> • Which economic sectors will create urban jobs and promote structural transformation? • Which economic sectors can create green urban jobs? • Which urban economic sectors have emerging growth opportunities under the AfCFTA? • Which economic sectors can create decent jobs specifically for women, youth and other disadvantaged populations? • Which economic sectors will leverage and harness urban demand for domestic sector growth? • How can cities add value to rural products through forward and backward linkages? • Where are firms and supply chains in priority sectors likely to be located? • What are the urban investment requirements specific to priority job-creating sectors? 	<ul style="list-style-type: none"> • What level of investment in urban infrastructure is needed to make cities major job creators? • Which urban investments and programmes should be prioritised to leverage urban economic advantages and align with national development priorities? • What components of urban management require national-level support and/or co-ordination? • Where should cities focus their priority: business retention or growth, or business start-ups? • What specific barriers do micro and small enterprises face? • Where do opportunities lie for productivity increase in the informal economy?





National spatial system	Co-ordination and finance
<ul style="list-style-type: none"> • Where, in the national spatial system, can investment achieve the most cost-effective, sustainable economic growth? • What kind of investments are needed to promote the economic growth of the “missing middle” size class of cities? • Where, within the national spatial system, will target economic sectors generate growth? • Which cities and towns require which types of intervention to support target economic sectors (combining spatial targeting and sector targeting)? • How can industrial parks and SEZs leverage existing geographic advantages for competitiveness and facilitate spill-over benefits to the rest of the economy and society? • How can connective linkages best bolster value chains and a productive system of complementary cities and towns? • What strategies are feasible to promote development of low population density and remote areas? • How may the African Continental Free Trade Area (AfCFTA) impact city size distribution, urban jobs and growth? 	<ul style="list-style-type: none"> • What level of government should have what function? • What are the legal powers that regional and local governments need to achieve their objectives? • What mechanisms can be established through the national development plan process to allow for co-ordination between the many public and private actors engaged in the development of cities? • What mechanisms can be established or strengthened to align economic planning, including implementation of AfCFTA, with urban and spatial planning? • How can subnational authorities be better supported to manage cities in ways that align with the national development plan? • Within cities and the national spatial system, how well is public and private investment currently co-ordinated and how can it be better aligned? • How can cities better leverage private sector contributions to investment? • How can the potential public revenue arising from cities be better harnessed for urban public investment? • What are the fiscal resources regional and local governments need to achieve their objectives?

Source (UNECA, 2018_[102]), An Urban Lens on National Development Planning in Africa: Guidebook for policymakers.

Sector targeting for job-rich urbanisation

Africa needs job-rich, sustainable growth. Its relatively strong GDP growth in recent years has been largely job poor. African countries need increasing productivity, while expanding decent employment opportunities, and there can be tension between the two. A key policy challenge is finding the right balance, depending on national economic realities¹¹ (AfDB, 2018_[110]). One of the central functions of national economic planning is to allocate resources to sectors that will drive employment-intensive and productivity-enhancing sustainable growth, while leveraging agglomeration economies.

Policy recommendations

1. Create decent employment at scale, by prioritising sectors with high urban employment effects and productivity potential.

Sectors vary in productivity and employment intensity, as well as in their urban location preferences. African countries¹² have adopted a new generation of industrial policies, with low-income countries focusing on light manufacturing (food, textiles, footwear, etc.), and middle income-countries in Northern and Southern Africa focusing on more technology-intensive and high-value added activities (Yong, 2014_[109]). Policies adopted in recent years in Ethiopia, Kenya, Ghana and Mozambique show renewed emphasis on promoting export in high-value agricultural and horticulture products, labour-intensive manufacturing sectors such as

clothing, textile, leather and leather products, through export-processing zones, industrial parks, financial incentives, capacity building, cluster development and direct public investment. Promotion of tradable services, including in finance, data processing, telecommunication and software development, is also an area of growing interest. Policy initiatives of some resource-rich countries target the development of domestic value chains in emerging and new industries, by linking domestic firms and foreign resource-extractive investors in the resource industry (Page, 2017_[110]). Targeted investment in infrastructure, technology and skills, and the potential role of regional integration and SEZs play an important role in implementing these policies and shaping urban space. Urban job creation should become a central theme within these priorities.

2. Address the discrepancy between formal and non-manufacturing informal labour markets by improving skills.

Workers in the informal economy have limited access to skills and training opportunities. The smaller size of most informal enterprises and their lower profits leave owners in the sector with fewer resources to invest in employees. Micro-entrepreneurs are often time- and resource-poor. Boosting productivity in the informal sector will require publicly funded training and vocational education and lifelong learning opportunities, in line with SDG targets. Paid time for training during working hours is a recognised step toward enabling gender-equitable outcomes, because women typically

bear the major responsibility for unpaid labour in the family and household out of paid working hours.

3. Increase firms' capacity to create jobs and boost productivity, by removing barriers to infrastructure and service provision, and modifying urban and land regulations.

Credit constraints and other barriers, including technology, hold micro- and small enterprises back from graduating to middle- and large-size firms. These issues should be addressed to unlock their capacity to create jobs, while increasing average firm size and productivity. Removing barriers that limit the growth of even small firms in low-tech, non-tradable sectors such as retail, transport, construction and food services could open up growth potential, with major effects on employment in the aggregate.

4. Pursue growth and employment opportunities in non-smokestack industries as an alternative pathway for structural transformation.

Invest in non-smokestack industries and in-service sector industries with wide multiplier effects on the productive sector, such as information technology, finance and professional services (Newfarmer, Page and Tarp, 2019^[81]). These sectors are crucial to the competitiveness of productive sectors including manufacturing, where service sector inputs account for a major share of the total value of the products, especially those for export.

5. Maximise the sustainable employment effect of the construction industry by leveraging investment in infrastructure and housing.

Unlocking the potential of the housing sector requires removing barriers in skills, housing finance, land and construction materials, such as cement and steel. Alongside job creation, early investment in sustainable construction and infrastructure will generate huge savings in energy and boost resilience. It is estimated that 900 million new urban residents will be added to African cities in the next three decades, and that two-thirds of the urban space Africa will have in 2050 does not yet exist. This means that African cities need to build twice as much, in one-third of the time that the existing infrastructure was built (Collier, 2017^[2]). Investing in cities offers vast potential for employment, including in green jobs and sustainable development.

6. Promote domestic sourcing of raw materials purchased by urban firms, particularly in sectors such as food processing.

The share of food purchased from modern retail (e.g. supermarkets) is rising sharply. The sector has

potential for major job creation in the food manufacturing and food services sectors, by increasing domestic agri-food value chain integration. Value addition and efficiency can be increased by reinforcing economic integration in the intermediating system linking food production and consumption. In addition, by lowering the cost of food in cities, efficient food value chains can help to increase the urban competitiveness of manufacturing.

Economically productive cities

Urban incomes are higher than rural incomes in Africa, as elsewhere. The gap is even larger at the household level, because a larger share of household members is in wage employment in cities than in rural areas. However, African cities have a long way to go toward realising their full potential for productivity and escaping a low-productivity equilibrium trap. Building productive cities requires good policies and plans, and adequate resources and institutional capacity to implement them. Managing urban growth in the context of rapid urbanisation, capital scarcity and capacity deficiencies makes the task particularly challenging. African countries should prioritise investment based on economic return and seek pragmatic policy solutions, which allow incremental improvement as resources and capacities permit.

Policy recommendations

1. Improve urban competitiveness through infrastructure and service provision, serving both firms and workers.

Urban infrastructure including electricity, communication, water and urban transport, affects the productivity of urban firms.¹³ Connectivity, by developing affordable, multimodal transport systems, should be prioritised in the urban development process. Without an accessible multimodal transport system, distance and cost price a large segment of workers out of the labour pool, while growing private car ownership increases congestion, air pollution and greenhouse gas (GHG) emissions. Efficient public transport benefits firm productivity, as it helps to counter the negative externalities of urban density, and thus reduce the urban employment cost (Venables, 2018). SEZs are one way to provide firms with a competitive business environment in the short term, when upgrading the infrastructure of an entire city is not financially feasible. These zones should be integrated with the urban labour market to take advantage of the productivity dividend of cities.

2. Promote cities as centres of innovation and competitiveness.

Africa’s economic future is tied to the ability of firms to innovate and compete in the local, regional and global markets. Countries vary in their industrialisation level and trajectory, with some aiming to acquire “traditional manufacturing capabilities”, while others turn to services, and still others promoting new and advanced types of manufacturing through local entrepreneurs (Naude, 2019). In all cases, innovation and technological upgrading plays an important role. Under the right conditions, cities facilitate firms’ access to technology, skills, capital and markets. They produce new ideas and are incubators for innovative firms. Developing this role requires a co-ordinated effort between levels of government, and engagement between the public and private sectors. National governments should invest in education and technologies such as information and communications, cultivate the role of cities as critical links to SEZs and universities, and as gateways to trade and foreign direct investment (FDI), and prioritise large cities as “nurseries” and hubs of innovation.

3. Promote effective land management systems.

Good land management systems promote sustainable urban development as well as trust in institutions and governance. Poorly managed land markets are a fundamental barrier to sustainable urban development in many African cities (Lall, Henderson and Venables, 2017_[26]). Meanwhile, a lack of access to well-serviced industrial land is a bottleneck for firm growth (Dinh et al., 2012_[21]). Multiple claims on land are common in many African cities, and speculation and title irregularities often prevent compact and connected development. As a critical asset, land is also associated with power and corruption, and suboptimal management can undermine trust in institutions and governance.

4. Promote practical planning and land-use regulations that support urban efficiency.

Planning processes and regulations, including land use and zoning rules, should not be burdensome. They should not limit firms’ and households’ choice of spatially efficient locations that balance the benefits and costs most important to the individual firm or household. Spatial layouts of cities should be evaluated in terms of whether they facilitate or deter proximity and connectivity between economic agents, and thus whether they increase or reduce agglomeration economies and well-being. Moreover, regulations on urban development should be responsive, enabling incremental development in sustainable patterns instead

of restricting or delaying private and household development of urban land. Regulations should also be practical, with adequate capacity to monitor and enforce planning regulations.

5. Strengthen the capacity of urban authorities in providing an adequate supply of well-planned, buildable and serviced plots within a network of connected streets and other infrastructure.

Finance may be a constraint in providing infrastructure at a high level of density and quality right away. However, it will be critical to provide space and demarcation to allow development of streets and infrastructure in the future, with incremental densification as a city grows economically. African cities are 23% more fragmented than Asian and Latin American cities (Page et al., 2020, p. 7_[28]), increasing travel times and infrastructure costs. Incentives should promote infill and discourage speculation, and serviced plots should be configured in a way that ensures good connectivity and enables incremental densification. Establishing settlements without a basic layout and street network can make service provision up to 12 times more expensive later (Campbell, 2018_[111]).

6. Promote an effective institutional framework to govern and co-ordinate large cities at the metropolitan scale.

Many big cities need a mechanism that co-ordinates strategic investment in infrastructure like transport, and that harmonises policies and regulations in urban planning and land use at the metropolitan level. As large agglomerations grow, a framework is needed to prevent unhealthy jurisdictional competition, promote efficient service delivery, and finance metropolitan infrastructure and services.

A connected national spatial system

Economic policies, whether fiscal, monetary or commercial, influence the location of investment and economic activities and help shape the national spatial system. Often, however, the interactions between economic policies and spatial outcomes are not fully understood or anticipated. Space-blind economic policies or spatial planning that is divorced from economic and social realities can have costly consequences for long-term development. This applies to sectoral priorities and location decisions regarding SEZs and industrial developments, for example. Opening up new regions for mining or massive agricultural projects, or investing in transport corridors to encourage trade with neighbouring countries, all have spatial

implications that need to be carefully assessed and managed. Directing investment to the sectors and urban agglomerations where economic return is highest, while managing trade-offs between efficiency and spatial equity, is essential to establish effective and connected systems of cities that allow for sustainable growth. Building a connected system of cities is a slow process, partly because it is path-dependent. A connected national spatial system to meet today's needs requires sustained implementation of coherent policies across sectors (OECD/UN-Habitat/UNOPS, 2021_[114]).

Policy recommendations

1. Target locations with sector policies, according to specific agglomeration economies.

Industries vary in their location preferences, depending on whether they benefit more from localisation or urbanisation economies. Industries with standardised production, especially those benefiting from localisation economies,¹⁴ benefit from relocation to cities with a high concentration of economic activity in the same industry, particularly to mid-sized and smaller cities that keep urban costs low. This leaves room for primary or large cities to specialise in industries and services benefiting from urbanisation economies (Henderson, 2010_[113]). SEZs should be connected to cities so that firms within them benefit from access to large labour pools; output and input markets; as well as industry-specific cluster benefits, while simultaneously, firms within the city benefit from the learning and knowledge spill-over effect of SEZs. In the short to medium term, it is important to invest in primary and large cities, because these cities will remain growth drivers for the foreseeable future.

Many primary cities in Africa are not large in global terms. The speed and scale of urbanisation in a context of low-income and lagging infrastructure development, however, makes it highly likely that continued investment deficits will have a negative effect on national GDP. At the same time, primary cities face increasing urban costs and congestion that need to be mitigated (Henderson and Kriticos, 2018_[72]). African countries need to maximise the productive capacity of larger cities, while slowly investing in intermediary cities and connectivity infrastructure. This will increase linkages between cities' economic activities and emerging growth centres, gradually establishing a functional urban system.

2. Encourage economic and physical connectivity of small cities in a larger urban sub-system and economic regions.

Given the large number of small cities, enhancing the role of small cities as agriculture service and primary agro-processing centres is an important step. Large cities are more productive than small cities, but smaller cities can become growth drivers, given the advantages of their amenities, quality of life and specialised economic functions. This report shows that rural economies close to cities perform better than those farther away. The closest urban area for rural residents typically has less than 50 000 inhabitants, underscoring the importance of small cities in encouraging linkages with agriculture, and in providing the rural population with access to services, infrastructure and markets.

3. Promote labour mobility.

Labour productivity and wages vary widely across space, reflecting differences in industry and firm productivity. Productivity levels would rise substantially if workers moved from low- to high-productivity areas, but this can be complicated by a host of factors, including government policy on migration; strong place-specific tastes; high housing costs and disamenities that can offset the appeal of the higher wages of productive urban areas (Glaeser and Xiong, 2017_[86]).

4. Invest in connective infrastructure, to strengthen links between cities and regional markets.

Many African cities are disadvantaged by geography, located far from seaports and international markets. This makes fast and efficient transport connections even more crucial. Connectivity is important both for export competitiveness and the price of imports, one of the factors that makes African cities disproportionately expensive. Inadequate transport infrastructure means that "trade costs in Africa are the highest in the world, stifling interregional trade" (Graff, 2018, p. 2_[114]). The continent also scores poorly on logistics, and its digital connectivity, while improving, lags behind that of other regions. Digital connectivity can lower economy-wide transaction costs, increase financial inclusion, improve market information, and provide access to opportunities in growing service sectors that are delivered online. Costs related to cross-border trade are significant, and improving intra-regional trade integration holds major potential benefits for urban production and consumption (see Chapter 2).

Financing policy implementation and co-ordinating urban and economic policy

Mobilising resources is essential for meeting urban financing needs. Effective implementation of national economic plans hinges on the capacity to allocate and enable absorption of these resources across sectors and levels of government coherently. Poor co-ordination is a fundamental problem that underlies many disjointed urban investment programmes and dysfunctional cities.

Policy recommendations

1. Mobilise domestic resources at the city and national level to meet cities' infrastructure investment needs.

Cities require massive investments, but they also generate enormous resources. An array of instruments is available to mine these resources, but applying them requires good governance frameworks and sub-national financial management capacity. Land value capture and leveraging the private sector are two entry points for improving resource mobilisation. No matter what financial instruments are used, there is a need for a substantial transfer of resources from the national level to meet the huge infrastructure investment needs of African cities.¹⁵ Most tax instruments are assigned to central governments, and many urban capital projects, for example transport and public transport infrastructure and communication networks, require large investments upfront before they increase public tax revenues. Prioritising cities in national economic planning and budgeting is thus central to realising the growth potential of urbanisation.

2. Address the technical and institutional capacity challenges facing urban project preparation and management.

African cities lack capacity to prepare bankable projects and to implement them within the necessary cost and time. Small cities may need investment facilities that can pool scarce expertise and resources and bundle projects. Financing models and governance structures are needed to help different cities in a regional or urban cluster implement joint projects, such as public transport or road development. Finally, it is important to complement megaprojects (e.g. regional rail lines, port or energy projects), with small, localised projects (e.g. housing improvement schemes and local

economic development initiatives), so local communities have access to the benefits of the megaprojects.

3. Co-ordinate investment between public and private sectors.

The government, firms and households need to co-ordinate. Cities generate externalities, and investments are discrete in time and space, creating an inherent need for co-ordination. Government, through its investment priorities in economic planning, can therefore crowd-in¹⁶ private and household investment. When public and private sector actors co-ordinate their investment, firms follow infrastructure, and workers follow firms, creating a virtuous dynamic for growth. When public investment is followed by private sector investment, the return to public investment is enhanced, and an economic base for local revenues and services is created. A co-ordinated investment in infrastructure, housing and jobs has a far greater economic return than the sum of the components. Some examples already show that countries can make faster inroads into new sectors by co-ordinating resources from both the public and private sectors. Ethiopia's success in breaking into the global market for cut flowers offers one example. Government and the private sector met regularly at the highest level to identify and address barriers, maintained a public record of actions and monitored progress systematically (Page, 2017_[110]).

4. Co-ordinate throughout the policy cycle at the vertical level, between national, subnational and sector levels; as well as at horizontal level across ministries, departments and agencies.

A mechanism to co-ordinate economic policies with urban and spatial policies is needed. For example, the AfCFTA implementation can create jobs in the tradable sector, but urban interventions are needed to boost the competitiveness of urban areas in which firms in the tradable sector are located. Mechanisms are context specific and cannot be prescribed, but in all cases, activities should be carefully sequenced; information and resource sharing should be encouraged; overlapping roles and responsibilities or mandates should be avoided; confusion and unhealthy competition or institutional rivalry between ministries, departments and agencies should be discouraged; and authority, resources and staffing to oversee processes involving a wide array of stakeholders, especially at the sub-national level, should be provided.

5. Establish spatially disaggregated economic and social data to support policy, including on economic and investment planning.

Addressing the policy issues and trade-offs discussed above and contextualising the policy recommendations proposed require reliable and geographically disaggregated data. Standardised spatial units should be established for this purpose. Spatial disaggregation of economic data takes time and resources. It should begin with basic statistics, such as employment

figures. Employment data by sector and cities, and firm size distribution by locations, are important to identify cities with potential for job creation and business start-up. Data on congestion, land market and housing will also be important, to track trends in urban cost and to detect fault lines in agglomeration economies. Data on urban investment against urban growth and metrics of access to services are necessary to monitor the capacity of cities to accommodate urban growth and demand by firms and households.

Notes

- 1 Building on what was originally proposed by United Nations Economic Council on Africa (UNECA, 2018_[62]).
- 2 "Space-neutral" policies deliberately avoid being place-based or location-specific. In a "space-blind" scenario, policy makers or planners fail to fully consider the spatial effects of their decisions in trade, industry and investment.
- 3 According to data from the United Nations Department of Economic and Social Affairs World Urbanization Prospects (UNDESA, 2018_[119]).
- 4 Youth unemployment is a particular concern. Youth unemployment in Africa ranges from 13% in Abidjan to 49% in Johannesburg (Metropolis, 2019_[59]).
- 5 Such as cut flowers.
- 6 As summarised in Chapter 1.
- 7 Here, urban infrastructure refers to infrastructure in cities, including connections to utilities. National infrastructure refers to infrastructure that goes beyond the geographic boundaries of cities (e.g. national power generation) or is measured at the national level.
- 8 Formally, it is normalised by the radius of a circle containing the same area as the city.
- 9 Urban primacy refers to the concentration of a country's urban population in a single city.
- 10 According to the Urban Centres Database (Florczyk et al., 2019_[122]), 40% of the population living in cities lives in primary cities in Africa, while the corresponding shares are 44% and 49% in Asia and Latin America, respectively.
- 11 Korea's employment elasticity of growth in its early stage of development and economic transition was 0.7; according to AfDB's estimate for the period 2000-2014, 18 of 47 countries in the sample (38%), had an employment-to-GDP elasticity of 0.41 or below. Another 20 countries (43%) had an elasticity of between 0.41 and 1.00 (AfDB, 2018_[10]).
- 12 At the national level, at least 26 African countries have national industrialisation strategies, and 19 of these strategies target light-manufacturing industries (AfDB et al., 2017).
- 13 As discussed in Chapter 1.
- 14 Localisation economies are the productive benefits for firms arising from same-sector clustering. Urbanisation economies are the productive benefits arising from the clustering of a diverse mix of firms from many sectors. Urbanisation economies are high in large cities, but mid-sized cities can achieve localisation economies without the costs of large cities.
- 15 "African cities are dependent on central transfers for more than 80% of their operating revenues, and local government revenues have been estimated to account for less than 1% of GDP (Venables, 2018, p. 93_[5]; Foster and Briceno-Garmendia, 2010_[115]). The per capita budget of African metropolitan cities is USD 177, compared to USD 1 359 in Asia and USD 1 053 for Latin America and the Caribbean regions. The per capita budget for the relatively prosperous cities of Durban and Johannesburg are USD 911 and USD 681 respectively (Metropolis, 2019_[59]).
- 16 Crowding in effect describes a circumstance in which government spending leads to an increase in private investments.

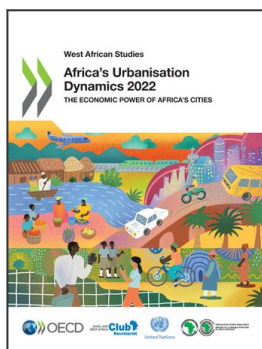
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From:
Africa's Urbanisation Dynamics 2022
The Economic Power of Africa's Cities

Access the complete publication at:
<https://doi.org/10.1787/3834ed5b-en>

Please cite this chapter as:

OECD/United Nations Economic Commission for Africa/African Development Bank (2022), "Anchoring the role of cities in national economic planning", in *Africa's Urbanisation Dynamics 2022: The Economic Power of Africa's Cities*, OECD Publishing, Paris.

DOI: <https://doi.org/10.1787/0248a1a9-en>

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