Building more productive, inclusive and sustainable cities

Policy and fiscal strategy

Malijeng Ngqaleni| National Treasury **|** 1 August 2017

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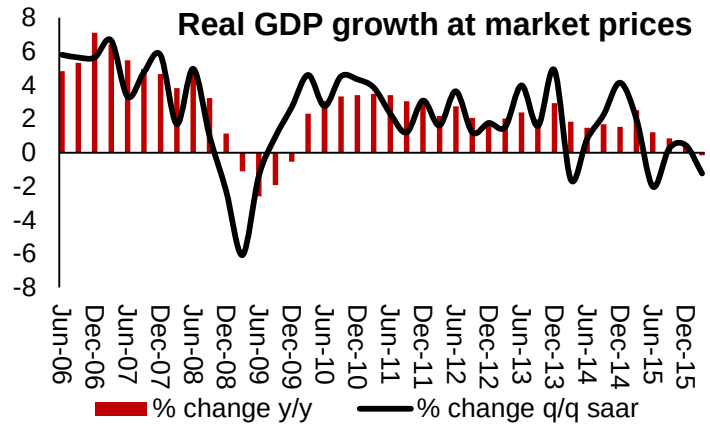
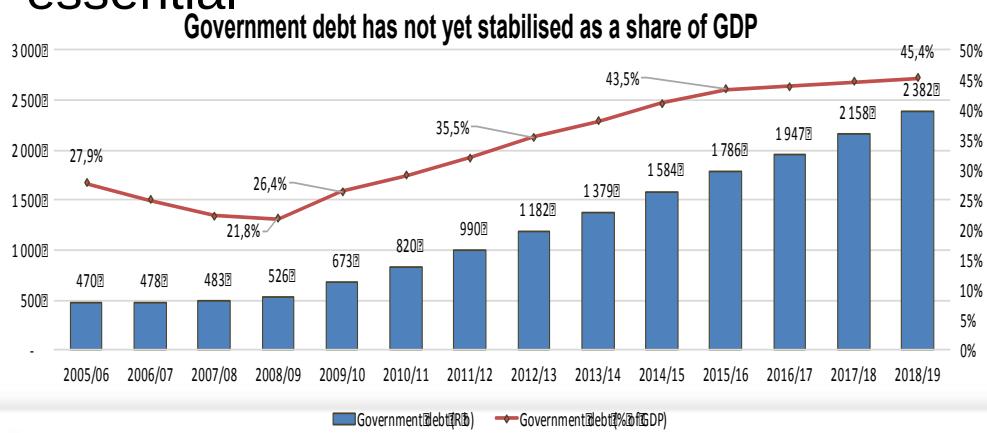
Objectives

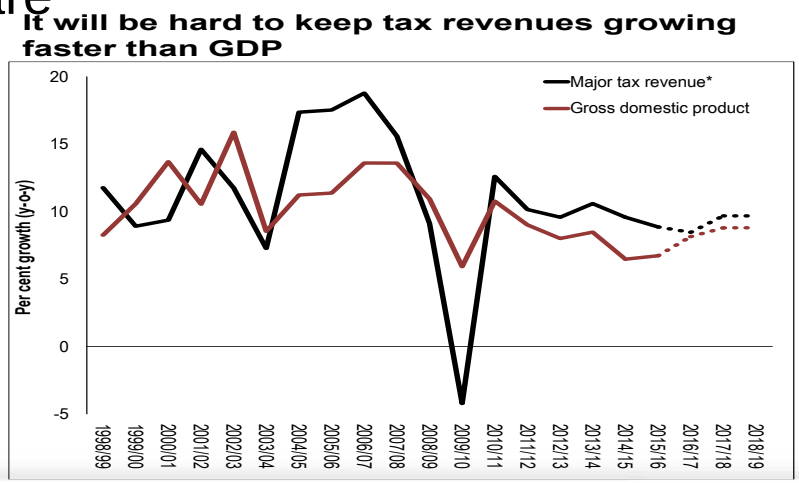
- Unpack urban development policy, strategy and programmes
- Identify key reform priorities
- Report on progress
- Clarify key implementation challenges

A difficult economic and fiscal context

- Weak growth
  - Underlying structural constraints are well understood, but require tangible progress
- Fiscal impact requires a programme of fiscal consolidation
  - Revenue impact, credit rating & public sector debt concerns
- Deep and practical partnerships across government and with the private sector are essential







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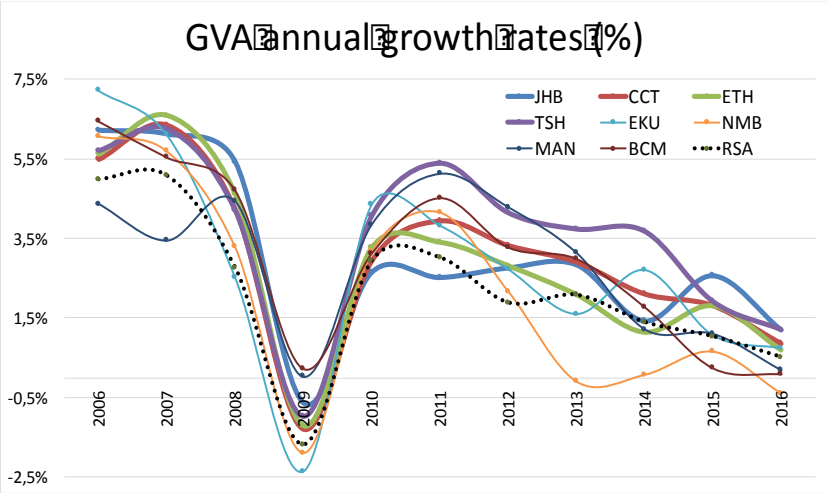
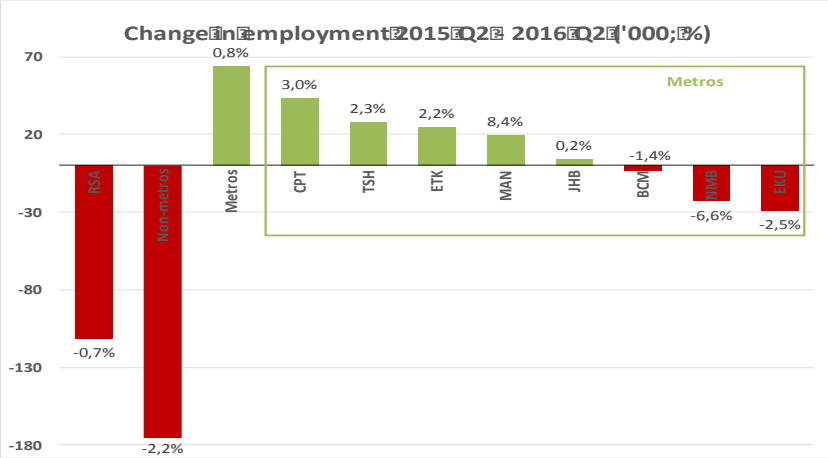
SA's urban powerhouses can drive growth and create jobs

- **Faster, more inclusive <u>urban</u> economic growth is essential for national development**
  - Both the SA economy and population are increasingly urban-based

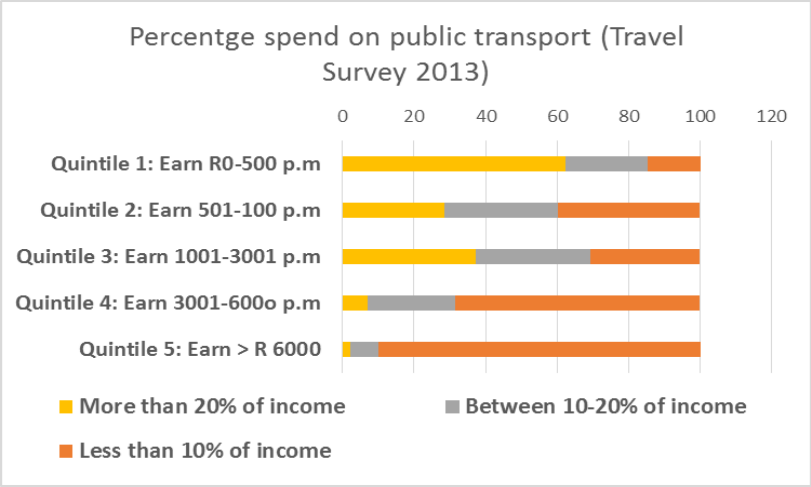
- **Urban centres are currently leading the economic recovery and job growth**
  - But SA is currently not fully benefiting from the "urban dividend"
    - » Urbanising poverty, not opportunity?

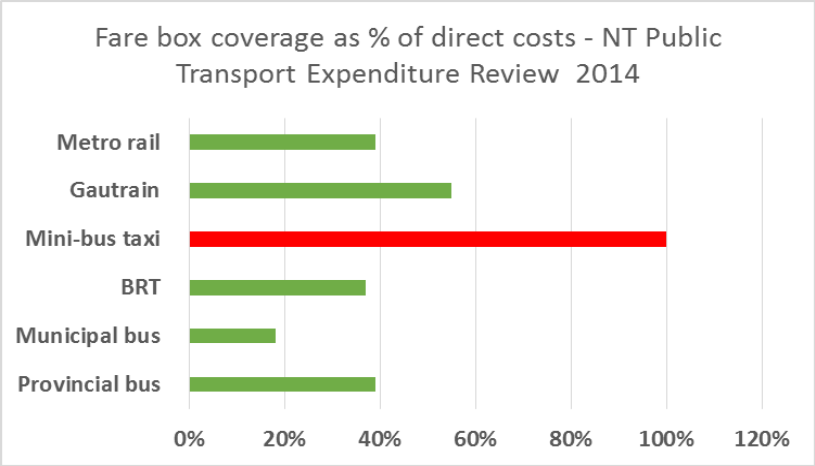




Despite significant progress in basic service access, large challenges in:

- **Service reliability:**
  - Poor asset management and maintenance
- **Housing affordability:**
  - Supply and demand constraints
- **Physical mobility:**
  - Transport under-investment and subsidy requirements
- *Growing "second generation" challenges:*
  - Urban resilience to climate change (droughts and floods)
  - De-coupling and technology change: energy and water
  - Fiscal sustainability: housing and transport

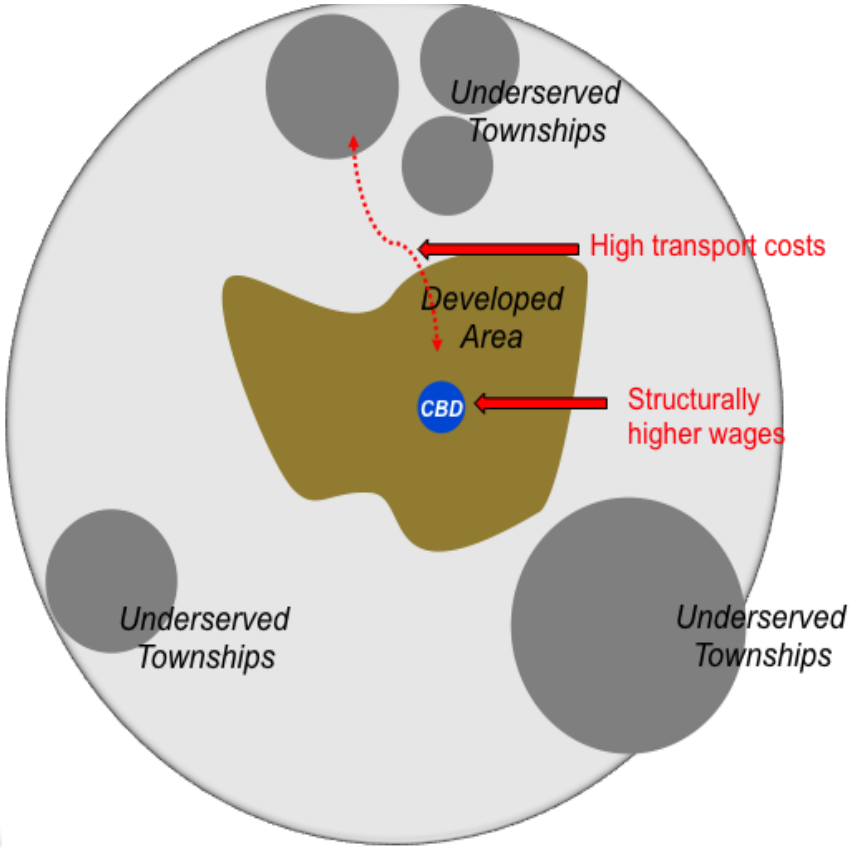




Spatial form is a structural constraint to growth

- Challenges are underpinned by **spatial fragmentation and low density settlement patterns** that:
  - Deepen inequality and exclusion
  - Constrain productivity growth
  - Weaken fiscal sustainability
- Current programmes deepen the fiscal challenge through addressing symptoms not causes
  - Low density, segregated cities are a reflection of the infrastructure investment and land use development choices we make

Many of our programmes are still structured to subsidise the low growth apartheid spatial legacy



... and most urban investment is driven by the private economic decisions of firms & households.

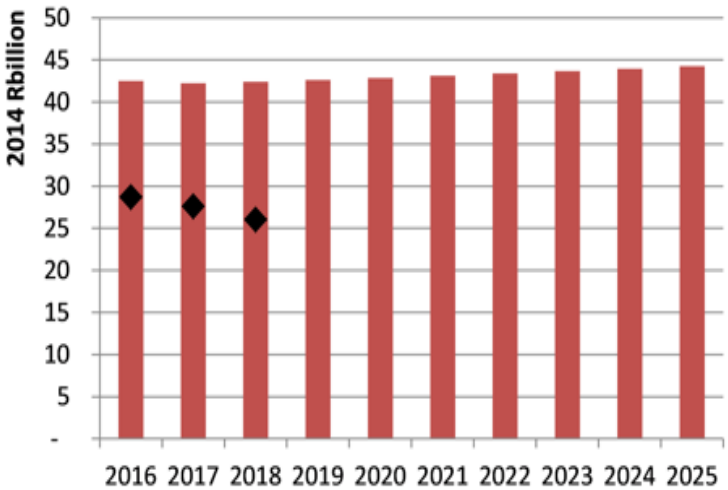
- **80%+ of national GDP is privately generated and funded (the ratio is even higher in the cities).**
  - Government strategies and actions to promote urban economic development and growth therefore necessarily operate indirectly.
- **The purpose of city activities to promote inclusive growth should therefore be to provide effective platforms for local economic activity**
  - Provide essential infrastructure & services for economic activity (growth platform)
  - ***Encourage the agglomeration and `connectedness'***
  - Improve the local business climate
  - Relate more productively with informal economic activities
  - Engage and establish partnerships with local business sectors

➢ **Requires coordinated action to realize this growth dividend**

SA cities have significant investment needs

- Large investments in urban infrastructure needed to unlock growth potential of cities
- Large urban municipalities have significant own revenues, established balance sheets, and significant managerial capacity
- Requires enabling cities to coordinate and lead planning and implementation management, and seek partnerships

Metros should invest an est. R43 billion / year to unlock growth



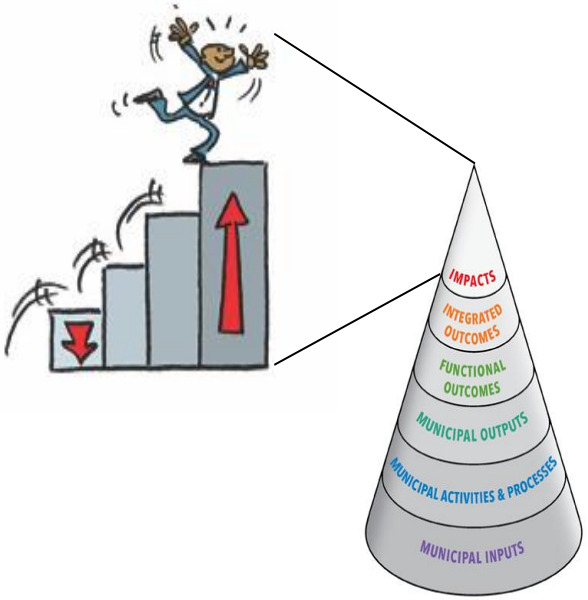
Rising returns on investment create a virtuous cycle of rising revenues and sustainable increases in expenditures

Metros face three major urban development priorities

- **Spatial integration** for the urban dividend to:
  - Expand access to affordable housing, in well-located, integrated human settlements
  - Improved mobility, through investment in and integration of public transport systems

- **Expanded investment** in core infrastructure to:
  - Support inclusive densification in targeted urban integration zones, universal access to basic services, asset refurbishment and replacement

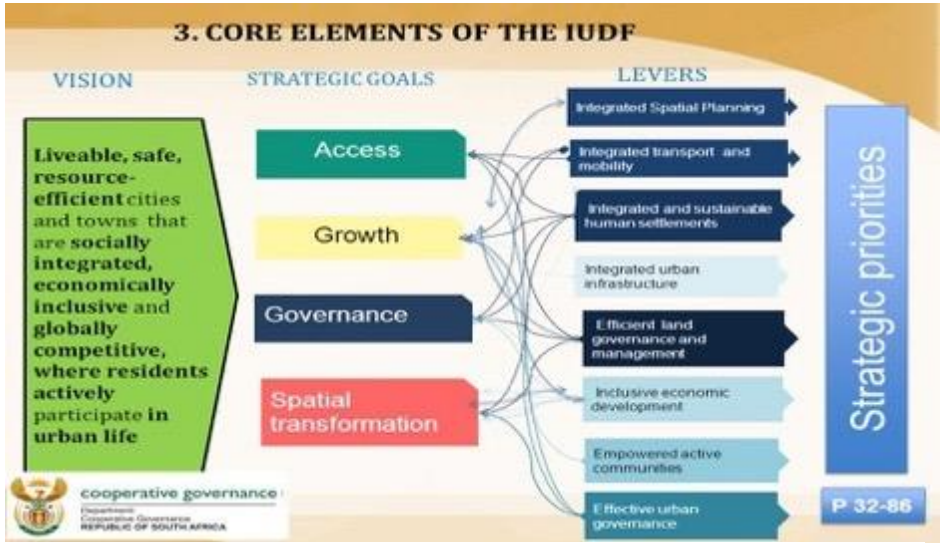
- **Deeper access to private financing** to expand resources available for investment through
  - longer tenure debt, broader participation (in more liquid markets) and innovation in financial instruments (eg TIF)
  - Less reliance on grants



Achieving outcomes requires leadership and partnership, but also delivery!

Driving spatial transformation for inclusive growth

- **Policy and legislative framework already in place to support this**
  - NDP & IUDF
  - Sectoral legislation
- **Measurable outcomes are agreed**
  - MTEF -> BE outcomes -> SBDIPs
  - Reporting reforms underway
- **Planning system significantly strengthened**
  - Outcomes led BEPPs based on clear value chain concepts
- **Need to deepen practical support to metro strategies**



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The Cities Suport Programme provides integrated implementation support to metros within this strategy

Innovative and appropriate practice gathered, generated and sharedâ

Support provided to cities in line with the BEPC

Leadership & governance support

Built Environment Performance Plans (BEPPs) and Capacity Support Implementation Plans (CSIPs)

Urban Management

Platforms convened for city advocacy and lobbying within the IG system & society

Component Plans

Core City | Human Se | Public Tra | Economic | Climate R

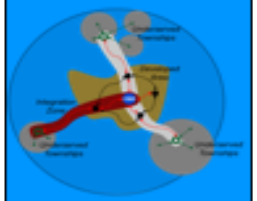
Well Governed Cities

- Vision & leadership to initiate & drive spatial restructuring
- Capability to plan & manage urban spatial transformation
- Partnership-based approach to the financing, packaging & delivery of catalytic projects in spatially targeted areas
- Delivery of catalytic projects in spatially targeted areas
- Citizen involvement in the delivery of projects in spatially targeted areas

Enabling Environment for City Transformation

- Restructured fiscal & financial framework to support urban growth
- Assignment of human settlements and public transport functions to cities
- Reviewed policy & regulatory frameworks that hinder cities in achieving their goals.

Compact Cities & Transformed Urban Space



- Established integration zones

Inclusive Cities

- New housing options with social diversity
- Affordable & efficient public transport services
- Integrated public transport system that is used by the majority of city inhabitants

Productive Cities

- Growing city economies
- Increased city productivity
- Increased use of renewables

Sustainable Cities

- Increased use of renewable energy
- Improved water resource management
- Resource efficiency
- Recycling

Urban economic growth and a reduction of inequality and poverty

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The Urban Network Strategy provides a common vision and framework for alignment

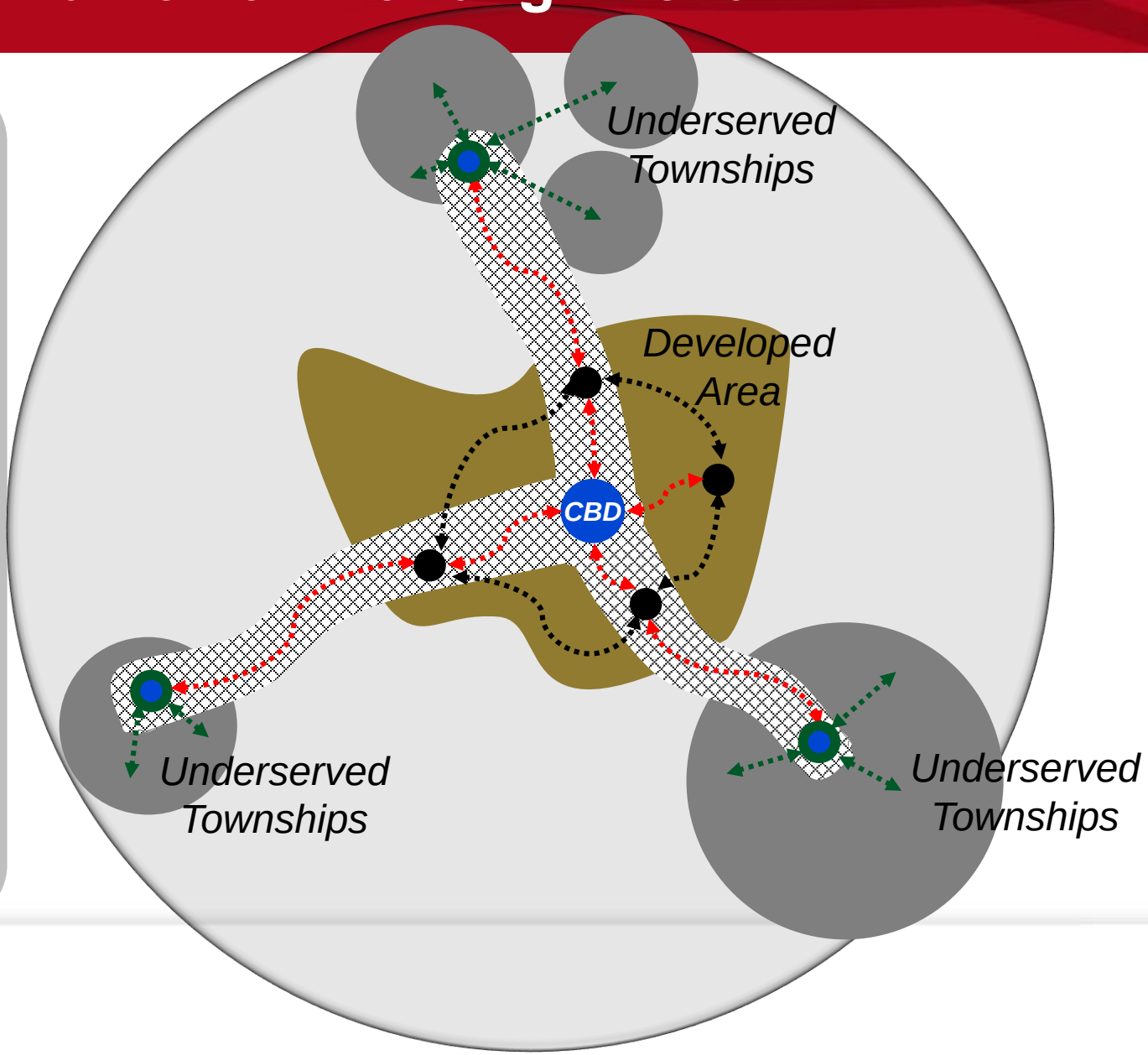
Spatially targeted investments by government:

Basic services and Human Settlements infrastructure in "integration zones"

Public transport networks

Targeted projects in new urban hubs

UDZ Development Incentives



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National government is introducing a more enabling policy and regulatory environment

Planning alignment	• Improve project disclosure (IRM) • Support development of Intergovernmental Project Pipeline by metros
Regulatory alignment	• Reviewing regulatory arrangements and obstacles • Streamlining and improved guidance on regulatory requirements
Fiscal reform	• Enable financial partnerships for development through borrowing, development charges • Support ongoing performance-based grant reforms • Housing and transport finance
Monitoring and Reporting	• Support outcomes-based rationalisation of indicators • Review and rationalise departmental indicators within outcomes framework

1. Planning Alignment

- **Properly sequenced investments across spheres is essential to building liveable cities, through creating agglomeration economies (”planning for people”)**
  - Currently very weak coordination between national and provincial investment programmes (including SoEs) with metro plans
  - Location and timing of investment programmes critical to creating liveable cities
  - Need to follow a systematic approach to planning, project identification and preparation across all spheres of government (ie BEVC)
  - Build Environment Performance Plan prioritized integration for targeted investments and alignment of planning across government
  - DORA requirements for BEPP and alignment of build environment grants – one plan considered by national departments for all the metro infrastructure grants aim to enable cities to integrate and align funding

Planning alignment: Metro's have all made good progress with urban network planning via annual BEPPs

FIGURE 9: Urban Network Strategy Framework

Source: NMBM, 2016

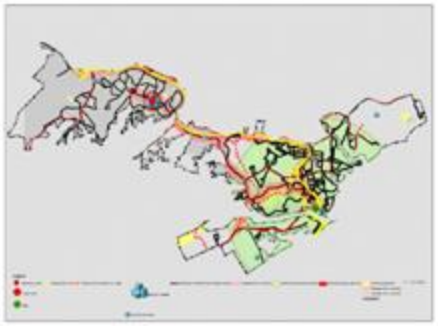
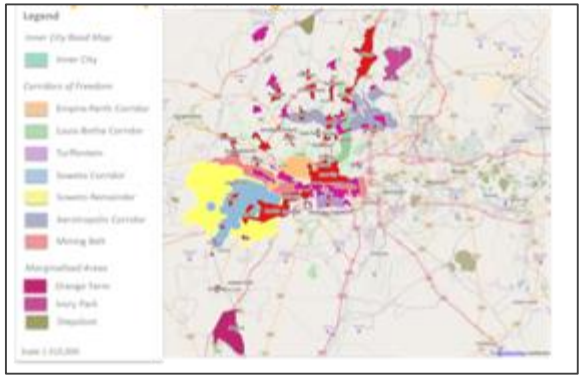


Figure B.2: Primary Integration Zone

Buffalo City Metro



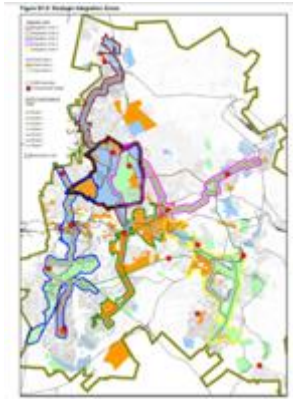
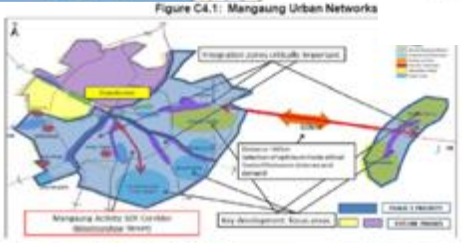
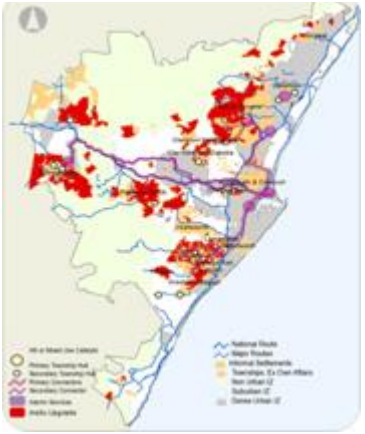
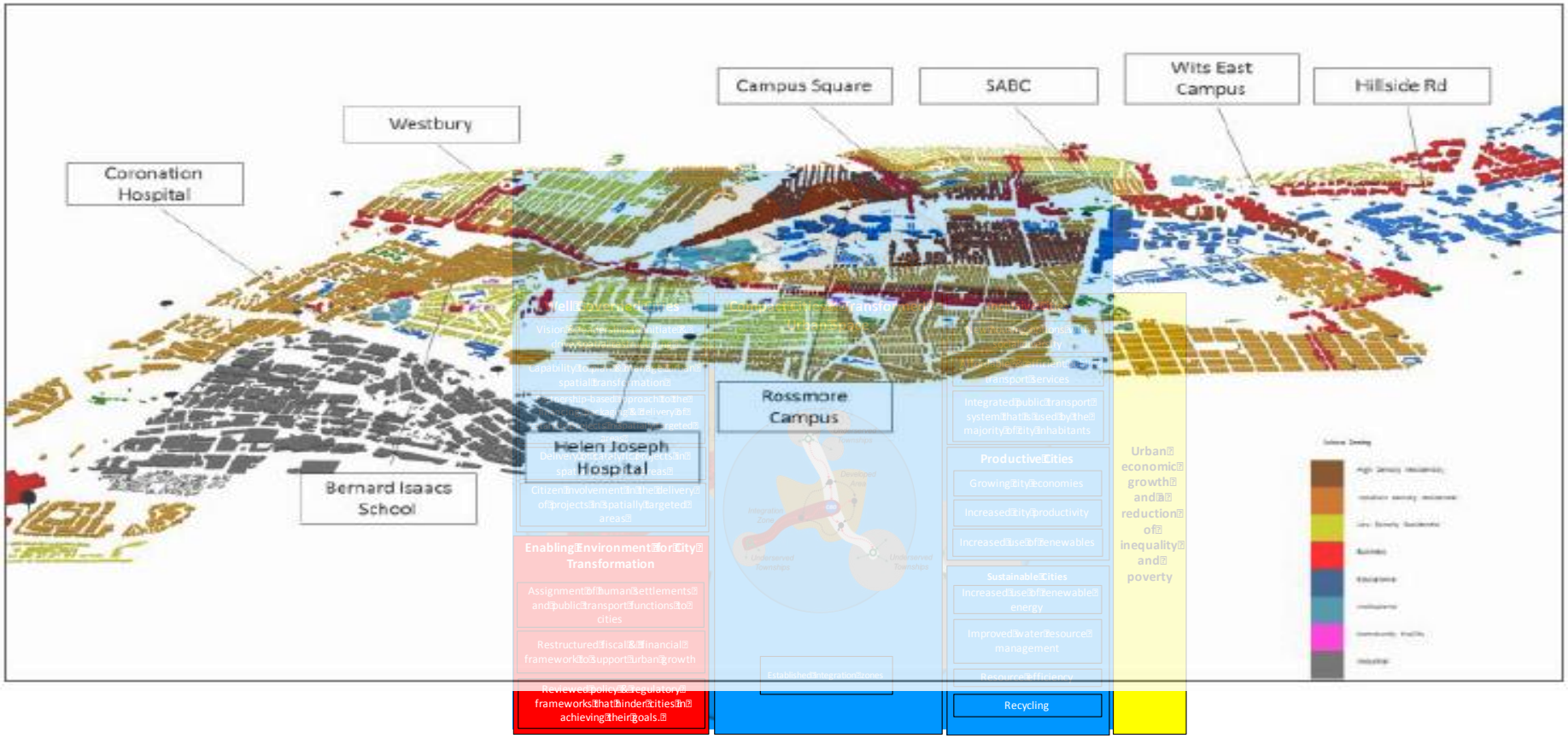


Figure C4.1: Mangaung Urban Networks





BEPPs show how government programmes can transform our cities over time … *if we align ourselves to required results*

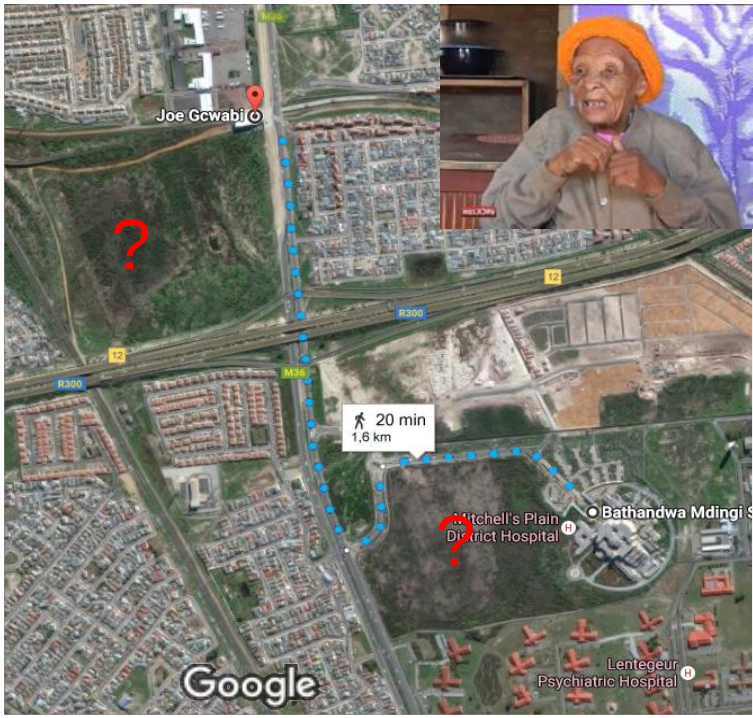


Planning Alignment: next steps

- **Two key steps:**
  - **a) Improve disclosure of investment pipelines ("what, where and when")**
    - Implementation of the Infrastructure Reporting Module (IRM)
      - Should disclosure requirements be strengthened in DoRA w.r.t. transfers
  - **b) Enhance sequencing of investments**
    - Develop a coordinated intergovernmental project pipeline
    - Strengthen coordination and approval requirements (portfolio management gateways)

2. Regulatory Alignment

- **Regulations, norms and standards impact on urban development:**
  - Increasing direct costs, costs of time delays, opportunity costs of sterilising land
  - Provide a framework for private investment
- **Review of urban infrastructure regulation underway to identify**
  - Shortcomings, duplication and costs associated with applicable regulatory frameworks
  - Potential institutional and procedural changes to enable faster delivery and better outcomes
- **Review of norms and standards** in specific sectors (health clinics, schools, libraries, roads, building code)
  - Standards appropriate for compact cities
- Strengthen the **use of land development rights** as a tool for urban transformation
  - E.g. Inclusionary zoning for affordable housing production



Regulatory reforms: next steps

- Deepen analytical work on spatial impact of facility norms and standards
  - Establish sectoral task teams

Fiscal reforms: SA has a well developed, robust local govt fiscal framework

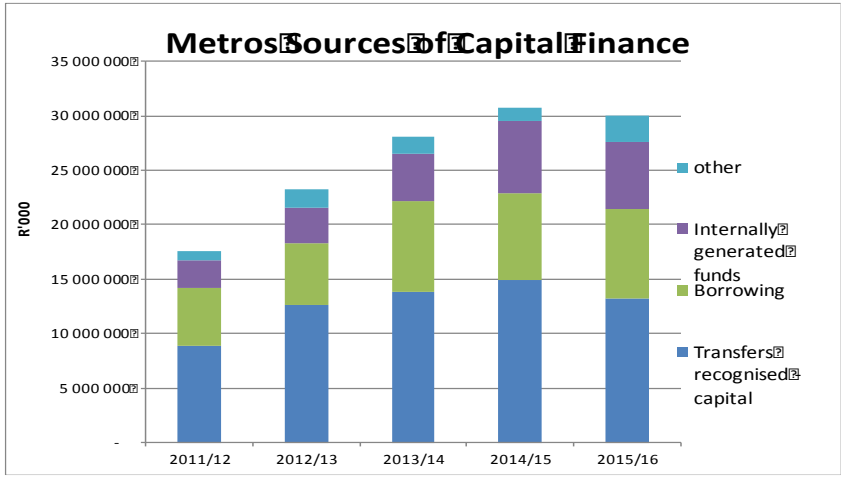
- Responds to basic functional assignments to municipalities, with appropriate fiscal powers
  - Significant own revenue powers (taxes and tariffs)
  - Autonomous borrowing powers
  - Citizen oversight

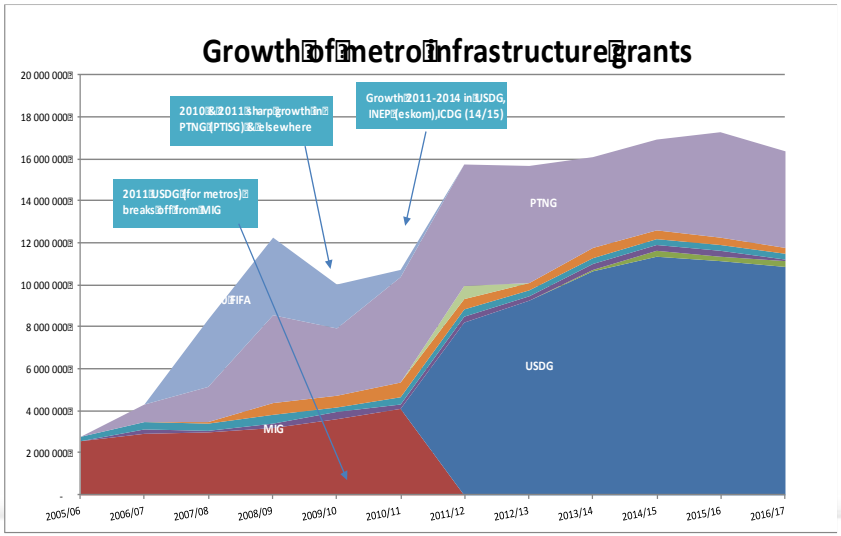
- National transfers provide a *differentiated* framework to address:
  - Redistribution and poverty
  - Structural vertical fiscal gap (between expenditure responsibilities and own revenue assignment)
  - National development priorities

- But, significant challenges with financing of concurrent functions of housing and transport

Fiscal reform and incentives

- **Spatial transformation for inclusive growth requires far greater leverage of private finance, aligned to metro balance sheets**
  - Grants cannot solve this issue - they must focus on:
    - Inclusion (redistribution)
    - Guaranteeing systemic stability & sustainability
    - Enabling performance
- **But growing problems with the grant framework for metros**
  - Grant dependence
  - Coordination (overlap and gaps)
  - Ongoing tensions over grant design
  - Expenditure performance
  - Weak grant administration (allocation, transfer, monitoring)





How much do transfers contribute to metro budgets?

Conrtibution of transfers to Metro budgets, 2016/17

R thousands	City of Johannesburg	City of Cape Town	eThekwini	Ekurhuleni	City of Tshwane	Nelson Mandela Bay	Mangaung	Buffalo City
Total Revenue (excluding capital transfers and contributions)	46 060 933	34 200 144	31 267 560	32 378 969	30 209 869	9 535 857	6 534 676	5 907 039
Equitable Share	3 182 318	2 012 945	2 319 380	2 381 367	1 864 838	798 043	524 776	678 197
% of operating revenue	7%	6%	7%	7%	6%	8%	8%	11%
Fuel Levy	2 595 595	2 197 740	2 185 002	1 625 872	1 440 100	496 799	272 691	410 031
% of operating revenue	6%	6%	7%	5%	5%	5%	4%	7%
Direct operating grants	66 363	57 206	79 028	38 175	53 122	24 046	23 517	11 488
% of operating revenue	0.14%	0.17%	0.25%	0.12%	0.18%	0.25%	0.36%	0.19%
Total grant funding as a % of operating revenue	19%	20%	24%	20%	20%	24%	27%	32%
Capital funding	9 543 581	6 501 277	6 725 067	5 130 961	4 465 209	1 416 400	1 806 094	1 558 134
Direct infrastructure grants	2 956 793	2 430 587	2 968 119	2 509 666	2 620 497	934 034	932 100	817 214
% of capital funding	31%	37%	44%	49%	59%	66%	52%	52%

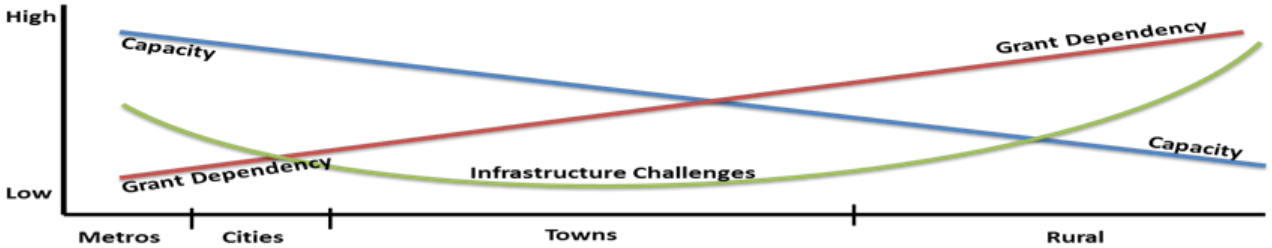
Source: NT Local Government database

- Transfers account for **more than 20% of operating budgets** for most metros
- Transfers account for a much **higher proportion of capital budgets** in all metros
- Smaller metros are much more transfer dependent
- City of Tshwane and Nelson Mandela Bay are currently grant dependent to fund capital budgets

Transfers supplement local sources of capital finance

- Need to expand sources of capital finance through:
  - Enabling responsible and sustainable borrowing by creditworthy municipalities:
    - Extending debt maturities, encouraging secondary market liquidity and providing a home for institutional investors
  - Encouraging use of other available sources of capital finance: land based financing
    - Reforms to re-regulate development charges
    - Innovations in limited recourse instruments (eg TIFs, SADs, development rights and PPPs)
  - Suggests important ***new*** role for DFIs
    - Market makers, not just participants

Agreement on long term differentiated vision for grants



A municipality's context should determine its grant system

Limit other grants to national priorities / regionally strategic projects (eg RBIG)

Consolidated Urban Grant
(limited input conditionality, supplements capital budget)

MIG
(allow municipal discretion, coordination with sectors, and emphasis on asset management)

Water & Sanitation

INEP

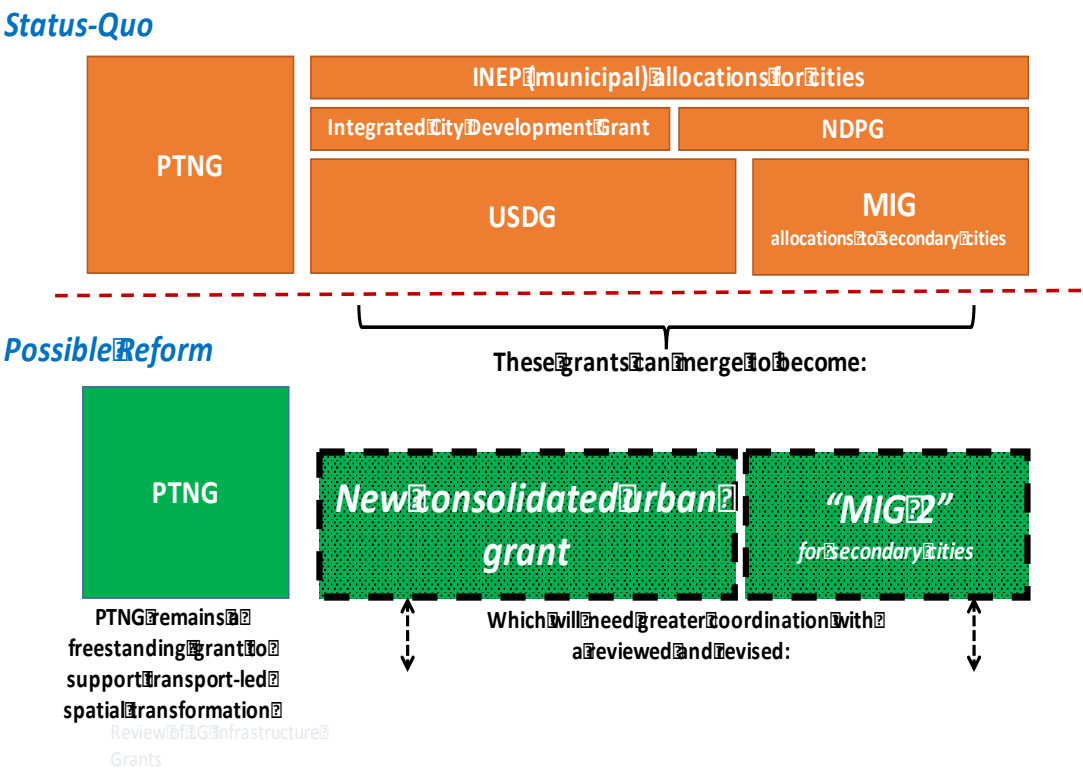
General Infrastructure & Community Services Funding

Metros | Cities | Towns | Rural

Extend metro grant reforms to some secondary cities over time

Progress with reconfiguring grants over the medium term

- **Progress with:**
  - Consolidated PTNG focussing on functional (mobility) outcomes
  - Consolidated urban grant (USDG)
  - MIG-2 for secondary cities
- **Medium term priorities**
  - **Expand performance-based grants** focusing on inclusive growth outcomes
  - **Improve grant administration** in design, reporting and evaluation
  - **Align other urban investments** in housing, transport, safety, health and education
  - **Deepen leverage of private finance** through improved proj preparation and appraisal



Specific recommendations

18/19 MTEF

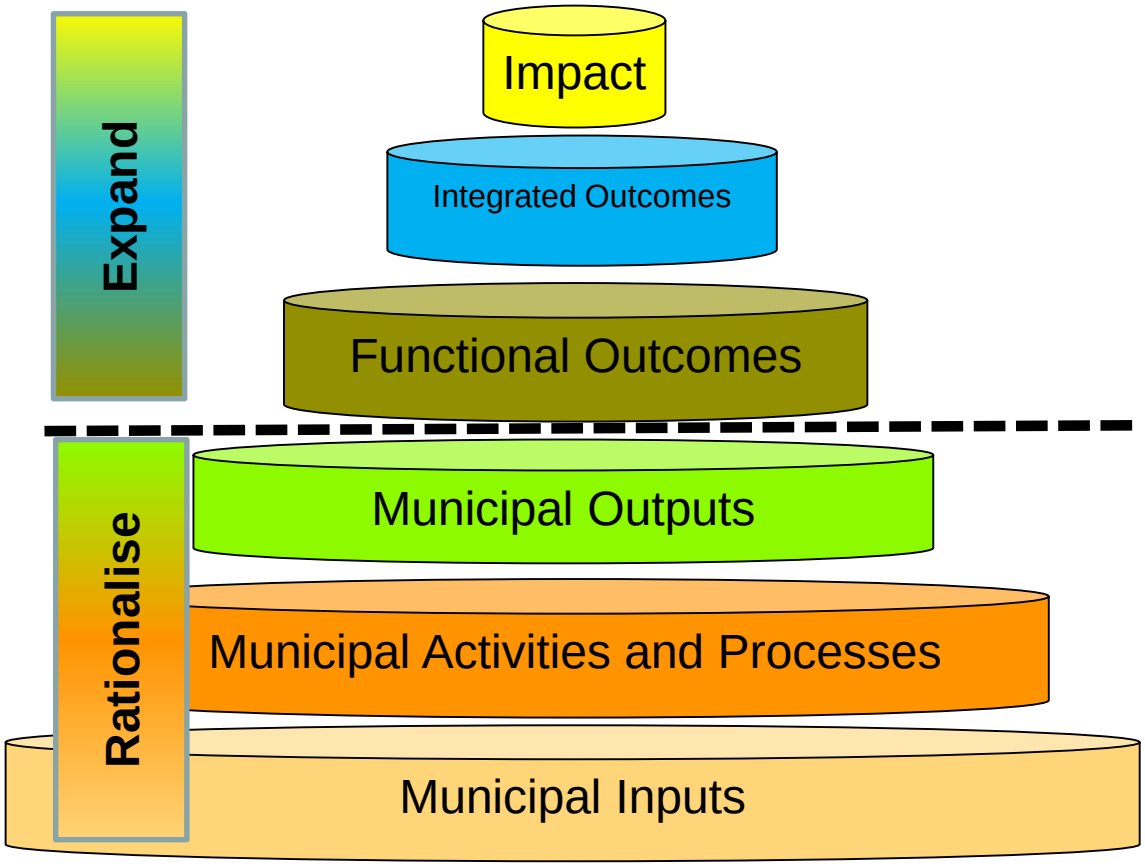
- **Restructure (and potentially reduce) total grant allocations to metros**
  - Expand performance "slice" of total allocations, based on common measures
  - Expand support preparation and implementation of all catalytic projects
- **Align grant frameworks**
  - USDG and PTNG to ensure focus on complementary outputs (within outcomes framework)

Medium term

- **Progressively align other grants (HSDG / Bus & Rail Subsidies) starting with:**
  - Improve disclosure requirements (including timing and reporting);
- **Align provincial planning and expenditure in metro jurisdictions**
  - Project disclosure requirements on common format (health, ed, etc)
- **Review grant administration capacity and organisational arrangements**
  - Ensure Depts play policy setting, oversight and evaluation roles
  - Professionalise grant admin over detailed design, allocation, disbursement, reporting and monitoring system

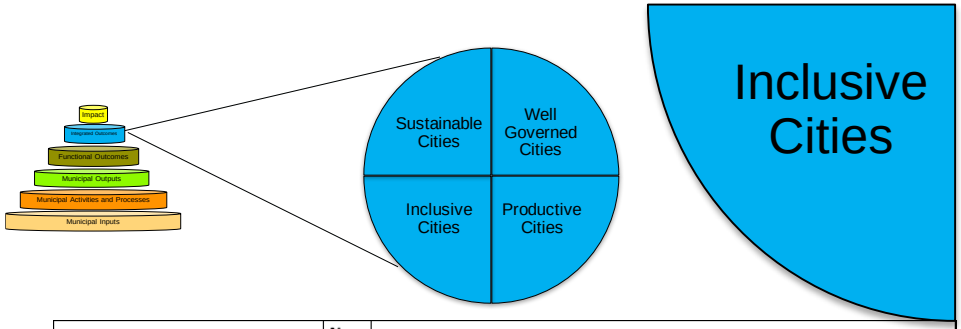
4. Monitoring and Reporting Reforms

- **Regular, credible reporting and monitoring of progress is essential**
  - "What you can't measure, you can't manage"
  - Key legal accountability requirement
- **BUT:**
  - We are measuring inputs, activities and outputs – but we don't know whether we are making a difference.
- **The response:**
  - Expand targeted BE outcome indicators
  - Rationalising indicators at the input, activity and output level, with a line of sight to outcomes
  - *Gentle pressure, relentlessly applied, within a coherent results based framework*



4. Progress with Reporting Reforms

- Progress to date
  - Common approach agreed (framework, principles and criteria)
  - Criteria applied to existing indicators from sector departments.
  - Integrated outcome level indicators piloted and finalised by cities through BEPPs
  - Leading a process to rationalise indicators at the input, activity and output level linked to the SDBIP.
    - Standardised templates and protocols.
    - Project completed by **Novembr 2017** (including an institutional platform).



What we want to see	New code	Indicator
New housing options with social diversity	IC1	New subsidised units developed in Brownfields developments as a percentage of all new subsidised units city-wide
	IC2	Gross residential unit density per hectare within integration zones
	IC3	Ratio of housing types in integration zones
	IC4	Ratio of housing tenure status in integration zones
	IC5	Ratio of land use types (residential, commercial, retail, industrial) in integration zones
	IC6	Informal dwellings in integration zones that have been upgraded, as a percentage of all informal dwellings in integration zones.
Affordable and efficient public transport services	IC7	Number of all dwelling units within Integration Zones that are within 500 metres of access points to the integrated public transport system as a percentage of all dwelling units within Integration Zones
	IC8	Percentage share of household income spent on transport costs for different household income quintiles city-wide
	IC9	Capital expenditure on integrated public transport networks as a percentage of the municipal capital expenditure
	IC10	Average weekday peak hour commuting time of passengers via the public transport system city-wide
	IC11	Average weekday peak hour commuting time of passengers from home to work or educational institution
Integrated public transport system that is used by the majority of city inhabitants	IC12	Percentage of commuters (city-wide) using private motorised transport
	IC13	Percentage of all passenger trips that use the same ticketing system
	IC14	Number of reported accidents involving cyclists and pedestrians city-wide per 100 000 population
Social facilities and services	IC15	Percentage of city-wide population within a 10 km of a local library
	IC16	Percentage of city-wide population within a 5 km of a clinic
	IC17	Percentage of city-wide population within a 5 km of a primary school
	IC18	Percentage of city-wide population within a 15 km of a Thusong service centre
	IC19	Percentage of city-wide population within a 5 km of an Early Child Development centre
	IC20	Percentage of city-wide population within a 5 km of a secondary school
	IC21	Percentage of city-wide population within a 30 km of district hospital.

Conclusion

- **Spatial transformation is critical** to enable our cities to become the engines of faster and more inclusive growth
  - This is a long term process, requiring a broad based strategy and deep, practical partnerships across society

- **National transfers must play an enabling role in this process:**
  - Must support integrated broader strategy and programme
  - Must enable metros to exercise their mandates effectively and accountably
  - Must leverage investment, rather than just execute projects
  - Must chase development outcomes, not just inputs