

DIRECTIONS in Urban Development

IMPACTS OF FINANCIAL, FOOD, AND FUEL CRISIS ON THE URBAN POOR

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Summary

- *The urban poor are particularly vulnerable in times of crisis due to their heavy reliance on the cash economy, job losses and wage reductions in urban based industries, and no agricultural production to fall back on.*
- *Prioritizing investments in cities can help to mitigate impacts in the short run and reduce risks in the future.*
- *Well targeted safety nets, workfare programs, and urban agriculture can play an important role in cushioning the impacts for the urban poor during difficult times.*

Introduction

The effects of the recent financial crisis are only beginning to be felt in many developing countries, but economic activity is declining rapidly with far reaching impacts. This crisis comes at a time when most countries are still struggling with the impacts of rising food and fuel prices. Though global food and fuel prices have softened somewhat in recent months from the highs earlier in 2008, there has been much volatility and they are anticipated to remain high over the medium term. It is estimated that the high food and fuel prices alone have increased the number of extremely poor in the world by at least 100 million.¹

While impacts of the crises affect both urban and rural populations, the urban poor have been hit hardest in this recent food and fuel crisis, and in previous financial crises, given their heavy reliance on the cash economy, no agricultural production to fall back on, and wage reductions and employment losses at urban based industries. This has resulted in social unrest in a number of cities earlier in 2008 all over the developing world.

The impacts on the urban poor are felt through a number of channels. With regard to food prices, the high costs directly hit the household consumption budgets of the poor as they are almost all net consumers. Higher energy prices result in higher production costs for a range of goods and services which use fuel such as manufactured goods, food, and transportation services though this impact is difficult to quantify.² The high costs also directly hit the urban poor through the extra cost of purchasing fuel. The proportion of

total household consumption that the poor spend on fuel is approximately 10% overall, and tends to be higher in urban areas. Higher prices may also cause households to move down the ladder of fuels which can have negative consequences such as indoor air pollution with increased use of biomass, and deforestation through collection of food (e.g. in peri-urban areas).

The financial crisis will affect developing countries and the urban poor through direct effects from a worsening economy and job losses in cities, as well indirect effects from reduced remittances, and the potential for reduced aid from donors. Countries will also face lower commodity prices, and may face a reduction in private investment flows, making weak economies even less able to cope with internal vulnerabilities and development needs such as infrastructure investments. The financial crises in East Asia and Mexico showed that urban households felt the impacts disproportionately. In Mexico's 1994/5 "peso crisis", urban households with workers in financial services and construction suffered the greatest income declines (48% and 35% respectively).

Those countries that have thus far been hit the hardest are those with large current account deficits, and for those that showed signs of overheating and unsustainable rapid credit growth prior to the intensification of the financial crisis. Of the developing countries whose economies have been hard hit, seven are in Europe and Central Asia, and eight from Latin America.³ It is anticipated that all countries will somehow be affected, though those whose economies are less integrated in the global economy will be somewhat less affected.

Impacts on the Urban Poor

Poverty

The existing evidence shows that the impacts on poverty from the food and fuel crises have been significant. The rise in food prices between 2007 and early 2008 were estimated to have increased the share of the population in East Asia, the Middle East, and South Asia living in extreme poverty by at least 1 percentage point. The impact on the urban

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poor was particularly acute, increasing the incidence of urban poverty by more than 1.5 percentage points in East Asia, the Middle East, South Asia and Sub-Saharan Africa.⁴

Many more people who are already poor are falling even more deeply into poverty. Recent back-of-the-envelope analysis using micro data for 72 countries estimates the impact of the rising food prices on urban poverty, and to what extent this is attributed to new poor, and to those that are already poor and become poorer.⁵ These estimates consider three alternative scenarios for food relative to price changes of 10%, 20%, and 30% during the 2005-2008 period. The analysis indicates that a 20% increase in food prices results in a 5.8% average increase in the urban poverty rate, using the US\$2.50 per day poverty line (which is arguably more appropriate in urban areas than US\$1.25 per day line), for the twenty most affected countries in the data set. The cost, estimated as the change in the poverty deficit, is on average 3.1 percent of GDP with close to 95 percent of this coming from income losses of those that were already poor before the price shock rather than those that are “newly” poor. Of those countries in the data set identified as most affected, eleven were in Africa, also included were the large South Asian countries and a few in Eastern Europe and Central Asia.

Vulnerable Groups

Those who are already poor who fall into extreme poverty are particularly vulnerable given that they have no reserves to fall back on if faced with further resource deprivation. Among this group, children are at highest risk of suffering irreversible damage to their health and education due to malnutrition, and dropping out of school to look for work.⁶ Extensive research on both malnutrition and low educational attainment show lasting impacts. Poor nutrition early in life retards child growth, cognitive and learning ability, educational attainment and eventually earnings in adulthood.⁷

There is also substantial evidence that poor women and girls are particularly vulnerable during difficult times. Within households, there is gender disparity as, “mothers forgo meals and in many countries boys get preference over girls.”⁸ A final vulnerable group in some countries is the elderly, particularly those living alone, as the financial crisis could jeopardize the security provided by their pensions and they may not have a safety net to fall back on.

Job Losses and Reductions in Wages

With the financial crisis, growth is slowing and exports from developing to developed countries are reported to be declining. This is likely to result in a reduction in wages and employment, particularly in urban areas, some pushing into poverty. In places such as Dhaka, Bangladesh, where many of the garment workers already fall below the poverty line, job losses or reductions in wages could result in higher levels of extreme poverty.

The recent reports of job losses in developing countries resulting from the financial crisis are mounting. In China, reduced foreign demand for Chinese goods has caused some closure and job losses in cities. “Companies have closed along the eastern coastal belt, with more failures expected over coming months, leaving Beijing increasingly concerned

about the implications for social stability. The official unemployment rate is expected to rise from around 4.0% now to 4.5% by year-end, with the overall situation worsening into the first quarter” (November, 2008).⁹ In Ukraine, there are reports of major layoffs of steel workers, real estate agents, and those in the banking industry (October, 2008).¹⁰ From Russia, “There are no hard numbers for how many have lost jobs since the country’s finances began shredding this summer.... Russian news media are filled daily with reports of layoffs. One poll released Monday (October) by the All-Russia Opinion Research Center found that 35 percent of Russians personally know people who have lost their jobs, with 10 percent saying they know of many” (October, 2008).¹¹ In Turkey, the automotive industry - one of the country’s largest exports - has been hit hard as a result of a reduction in European demand with a number of plants cutting production (November, 2008). In India, there are projections of major job losses as a result of the crisis particularly in construction, real estate, financial services, and the auto sector (November, 2008).

Remittances and Migration

Remittances are a major source of income for many countries and play an important role in poverty reduction. For example in Nicaragua, remittances reduce poverty incidence by four percentage points on average, and five percentage points in urban areas. Remittance flows from host to developing countries began slowing in the second half of 2008 and are projected to drop sharply in 2009. All regions are expected to be affected. Latin America and the Caribbean are highly dependent on remittances from the U.S. and are likely to be hit hard. In 2007, India, Mexico and China were the top three recipients of remittances. And in some countries, such as Tajikistan, Moldova, Kyrgyz Republic and Honduras, remittances account for more than 25 percent of the countries GDP.¹²

Reverse migration is to be expected both from urban to rural areas, and from developed to developing countries as workers cannot find employment. Reversals of rural-urban migration patterns were observed in Indonesia and Thailand during the East Asian Crisis and for countries of the former Soviet Union after the Russia Crisis. While this will reduce some of the excess supply of labor in cities, it may then be offset by migrants returning home from abroad. This means not only a loss in remittances, but in some cases additional workers looking for jobs in a slow economy. In Mexico City, the Municipal Government predicts that “between 20,000 and 30,000 more immigrants will return for good from the United States during the Christmas holiday because they cannot find work” (October, 2008).¹³

Social Impacts

Urban areas tend to be more prone to stark inequalities and problems of crime and violence. The high food and fuel prices have resulted in widespread reports of social unrest in cities earlier this year in countries as diverse as Haiti, Mexico, Peru, Egypt, Morocco, Afghanistan, Yemen, Bangladesh, Burkina Faso, Cameroon, Senegal, Mauritania, Mozambique, Guinea, and Indonesia. Reports of riots, property destruction and even death have prompted a range of Government responses.

Reports of Recent Social Unrest in Urban Areas Due to Rising Prices

Mexico City, Mexico

“In January 2007, the ‘tortilla riots’ broke out in Mexico City. 70,000 people rioted against increased corn prices.”¹⁴

African Cities

In February of 2008 riots broke out in three major towns in Burkina Faso – Bob, Ouhigouya, and Banfora – in response to rising prices of food, clothes, and gasoline. Government buildings were destroyed and many injured. Protesters blamed government’s recent crack-down enforcing collection of custom taxes from merchants importing food and the global rising wheat prices.¹⁵ Government announced it would lower taxes on basic goods by 30-35%. Riots broke out in Cameroon a few days later instigated by taxi drivers over fuel prices that escalated into a protest over food prices followed by riots in Senegal and Mauritania.¹⁶

Port-au-Prince, Haiti

In April, 2008, major riots occurred in Port-au-Prince in response to increased food prices lasting over a week and resulting in the resignation of the Prime Minister. The price of rice, beans, and fruit, among other staples, increased by 50% in a one year period.¹⁷ Food shortages and starvation are becoming widespread as residents eat clay mixed with butter and salt to fight hunger. Haiti implemented a temporary response using international aid money and price reductions by importers to cut the price of a sack of sugar by 15%.¹⁸

Mahalla El-Kobra, Egypt

Riots broke out in the Egyptian industrial city in the Nile-Delta, Mahalla El-Kobra, for two days in April 2008 with rioters protested high food prices and low wages. As an immediate response, Government is giving bonuses of 30-days of wages to workers.¹⁹ In response to increased prices in wheat, Egypt subsidizes its bread – however lines for subsidized bread are increasing and corrupt bakers try to sell subsidized flour on black market for higher prices. As a response to the shortage of subsidized bread, the Egyptian military is being put to work to bake bread.

Dhaka, Bangladesh

On April 28, 2008, 20,000 textile workers protested rising food prices in the outskirts of Dhaka. Bangladeshi officials launched a rural employment program for the poor in response.²⁰

Responses to the Crises, an Urban Perspective

The approach to the crises adopted by the World Bank has been to substantially increase financial support for developing countries that will protect the poorest and most vulnerable from harm, support countries facing big budget short-falls, and help sustain long-term investments upon which recovery and long-term development can be built. These include productive investments in infrastructure, health and education, and in social safety nets for the most vulnerable. Many countries have responded to high food and fuel prices through tax reductions to offset higher prices and increased spending on subsidies and income support. These programs, however, are regressive, expensive, and very difficult to remove once in place.

The principles for designing policies and programs for addressing shocks do not differ for the rural and urban poor. Public investment in infrastructure has shown to

have long term economic benefits and generates employment. Investments in health and education build human capital, and will mitigate the potential long term negative consequences of malnutrition and school drop out. Well-designed, targeted safety nets can cushion the impacts on the poor, enable households to maintain a basic standard of living, and curtail social unrest. Finally, there is much evidence that urban agriculture can also help to mitigate the impacts of crises through the production of additional income and food for households. Implementing such strategies in urban areas will require a concerted effort and good collaboration between national and local Governments.

Maintaining Investments in Cities

Lessons from previous crises highlight the importance of safeguarding investments in long term development.²¹ This includes investments in infrastructure as is outlined under the World Bank Sustainable Infrastructure Action Plan (SIAP) as well as in human capital. Cities rely on infrastructure for economic growth and poverty reduction, and on a well-trained, healthy workforce. Within this context, targeting investments for the poor during times of crisis, and using labor intensive approaches as is done in workfare programs can help to mitigate impacts in the short run as well as reduce risks in the future. Programs such as slum upgrading which invest in providing water and sanitation, electricity and roads to the urban poor, and investments in basic education, health and nutrition in low income urban areas, have demonstrated long term benefits for the poor.

Social Safety Nets for the Urban Poor

The type of safety nets available in urban areas varies substantially from country to country and even city to city, with some operated through national level programs, and others operated more locally. While it is difficult to quantify whether there is an urban or rural bias in these programs, in many places the proportion of poor is often higher in rural areas and thus programs are oriented accordingly. It can also be difficult to reach the urban poor as they often live in informal settlements and tend to be more transient than rural populations. Among the more popular safety net programs are Conditional Cash Transfers (CCTs), workfare programs, fee waivers, and targeted cash or in-kind transfer schemes (e.g. food distribution, food stamps, or vouchers) all of which could be scaled up in urban areas during times of crisis.²² It is naturally easier to scale up an existing safety net program than to design a new one, but some countries have been able to use a crisis as an opportunity to eliminate ineffective programs and replace them with better designed programs.

Conditional cash transfers are particular relevant in times of financial crisis when poor families may deem it necessary to withdraw children from school to seek employment. By providing some incentive to keep children in school and provide a transfer to households, there is substantial evidence that the CCT approach results in short term as well as long term benefits from the additional schooling and health care. CCT program design in urban areas must face challenges different from rural areas in targeting due to more heterogeneous neighborhoods, informality of jobs and housing, and feasibility of using banks for transfers.

Workfare programs or labor intensive public works projects can also be particularly effective in urban areas to provide income support and employment, provide some on-the-job training for unskilled workers, and construct or rehabilitate public infrastructure. A well known workfare project is Trabajar in Argentina which was set up following the peso crisis (1999) and invested in small scale community projects. The program targeted poor households by use of a low wage rate, supplemented by a project selection process that geographically targeted poor areas to receive projects. The basic principles of the workfare programs do not differ substantially from some of the urban upgrading or community development projects. The Urban Poverty Project in Indonesia was originally set up following the 1997 financial crisis and was designed to improve basic infrastructure in poor urban neighborhoods and to promote sustainable income generation for poor urban residents who had been affected by the economic crisis. It was not exclusively set up as a workfare program but the infrastructure grants component had similar objectives and outcomes. The program was seen to have achieved its goals and has continued with an expanded and longer term approach to addressing urban poverty through community interventions. Similarly, current and planned slum upgrading programs can be designed to achieve short term income transfers through labor intensive works, and longer term investments in community infrastructure.

Scaling up Urban Agriculture

Urban Agriculture can be a very important source of additional income and food for households. It can reduce consumption of more expensive imported food products, reduce transport costs, provide products that are highly perishable, generate income and employment, and have important impacts on environmental sustainability. It is estimated that some 15% of the world's food is produced in urban areas and this could be scaled up even further, with huge potential benefits for the poor. More recent estimates for West Africa, for example, suggest that at least 20 million people—of an urban population of 100 million—live in urban households engaged in different forms of urban agriculture. In many cities they produce 60% to 100% of the consumed perishable vegetables. Many of the subsistence farmers are women, operating garden plots that often are in low-density, illegal or informal settlements.²³

There are currently a number of initiatives to scale up urban agriculture in countries as diverse as Sri Lanka, Argentina, Brazil, Mexico, Sierra Leone, South Africa and China. This requires investments by municipalities in

ensuring safe production to mitigate health and sanitation problems caused by wastewater, the use of chemical fertilizers and waste from animals. It also requires some oversight that urban agriculture is located on appropriate lands and does not interfere with land and housing markets. The World Bank and donors can help by providing technical assistance, and necessary infrastructure investments through our urban and other relevant projects.

Endnotes

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