

Towards foreign direct investment for development in the host state? Revisiting charter cities

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WTI Working Paper No. 04/2022



D UNIVERSITÄT BERN

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Introduction

Foreign direct investment (FDI) is undeniably one of the drivers of economic development in the host state. To this end, while investors seek rent in the host state, the host expects economic growth from FDI, particularly job creation, transfer of skills and technology, foreign currency and industrial development.¹ It is for this reason that states entered into a race in concluding international investment agreements (IIAs) with a view to signal to the investors their openness to FDI while guaranteeing legal certainty that investors need especially in extractive industries. Not only have states concluded IIAs with a view to attract FDI to stimulate economic growth, they also offered incentives such as tax free holidays, promise of cheap labour, visas and others to investors.² Important to note is that all countries, irrespective of their economic development, engage is some form of investment promotion because of the importance of FDI in ensuring sustainable economic growth.

Whereas FDI remains concentrated in the developed economies,³ there is considerable amount of FDI that trickles into Africa especially in the rich resources-based economies such as Nigeria, Democratic Republic of Congo (DRC) and South Africa.⁴ However, the levels of poverty remain unabated, as the top ten countries with highest levels of poverty are African including South Africa.⁵ Further, world unemployment rankings list many African countries in the top ten, at double-figure digit as high as 77 per cent for Burkina Faso and many of them

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¹ JE Alvarez, The Public International Law Regime Governing International Investment (Hague Academy of International Law The Hague 2011), 132.

² David Lim, 'Fiscal incentives and direct foreign investment in less developed countries,' (1983) *The Journal of Development Studies*, 19(2), 207-212.

³ FDI remains concentrated in the developed world largely because the 21st century market economy is driven by high tech products, which are manufactured and consumed in the developed world. Therefore, it makes economic sense that investors would setup in countries where there are skills and purchasing power to consume the products. Developing countries, especially in Africa, are still focusing on commodities and not integrated in the value chain – it is for this reason that FDI remains scarce to these countries.

⁴ 'Regional FDI at the glance: Africa,' available at <u>https://unctad.org/system/files/non-official-document/Regional_FDI_at_a_glance_Africa.pdf</u>, accessed 15 October 2021.

⁵ 'Poverty rate by Country 2021,' available at: <u>https://worldpopulationreview.com/country-rankings/poverty-rate-by-country</u>, accessed 15 October 2021.

around 40 per cent of poverty levels.⁶ The amount of FDI that South Africa, Nigeria and DRC attract indicates that transfer of wealth and skills alone is not enough; rather, there must also be political and social institutions that will channel the skills and wealth towards development.⁷

Africa remains largely a crisis continent with poor institutions to ensure adherence to democracy; corruption is bread and butter, crime is debilitating, malnutrition and diseases have become synonym to Africa, while poverty is rampant. ⁸ Africans who are closer to Europe have embarked on mass illegal migration and perish in the high seas while those that are able to make it to Europe have become a humanitarian crisis because the system is not prepared for them.⁹ Others embark on intra-continental migration and flock to countries such as South Africa where there is contestation for opportunities with the locals, which then escalate into xenophobic attacks because the system is not prepared for this kind of migration.¹⁰

Out of humanity, developed countries provided aid, sometimes with conditions while other times with no conditions, which have mostly done nothing to change the situation.¹¹ In most cases, projects are abandoned once the funder leaves.¹²

Equally, many African countries developed industrialisation policies to stimulate job creation and economic development. However, the results remain unnoticeable because of many problems, which include the following: corruption; new jobs not proportionate to job-seeking population in the industrialising location; residents not having skills required in the job market; and, firms located too far away from home for some workers.

As some have indicated, we have options of expanding the current cities or creating new ones to respond to challenges of economic development.¹³ However, expanding existing cities is problematic structurally and otherwise. To this end, most cities start to decline due to over-population, as it is the case of the Johannesburg

⁶ 'Unemployment by Country,' available at: <u>https://worldpopulationreview.com/country-rankings/unemployment-by-country</u>, accessed 15 October 2021.

⁷ Rahul Sagar, 'Are Charter Cities Legitimate?' 2016 Journal of Political Philosophy 24(4), 509-529, 509.

⁸ Robert Guest, *The Shackled Continent* (Pan Publishing, 2015); Paul Collier, *The Bottom Billion* (Oxford University Press, 2008); Chika Onyeani, *The Capitalist Niger: The Road To Success – A Spider Web Doctrine*, (Jonathan Ball Publishers, 2012).

⁹ James Hampshire, 'Europe's Migration Crisis,' 2015 *Political Insight* 8-11; Jeanne Park, 'Europe's Migration Crisis,' available at: <u>https://scholar.google.co.za/scholar_url?url=https://www.pravo.unizg.hr/_download/repository/semiunar_migrants.docx&hl=en&sa=</u> <u>X&ei=HKKCYa2BCrGUy9YPq6mjyA0&scisig=AAGBfm1_jWw0ctZytoYU7yLZGuYBLS8GAg&oi=scholarr</u>, accessed 17 October 2021.

 ¹⁰ <u>Godfrey Mulaudzi</u>, <u>Lizette Lancaster</u> and <u>Gabriel Hertis</u>, 'Busting South Africa's xenophobic myths starts at grassroots' Institute for Security Studies, 12 April 2021, available at: https://issafrica.org/iss-today/busting-south-africas-xenophobic-myths-starts-at-grassroots
 ¹¹ N. Hermes & R. Lensink 'Changing the Conditions for Development Aid: A New Paradigm? (2001) *Journal of Development Studies*, 37(6), 1-16; M. McGillvray & O. Morrissey, 'Aid Illusion and Public Sector Behaviour' (2001) *Journal of Development Studies*, 37(6),

<sup>118-136
&</sup>lt;sup>12</sup> Chima Okereke, 'Causes of failure and abandonment of projects and project deliverables in Africa,' (2017) *PM World Journal* 6(1), 1-16.

¹³ Matt Coetzee, 'Charter Cities: What if we could start from scratch?' 2017 Construction Research and Innovation 8(4): 117-120, 118

city centre, which saw dramatic decline from the 1980s and investors losing value of their existing properties.¹⁴ It becomes a vicious cycle of decline and poverty because businesses are located in the cities, and when the city declines, not only do the existing investors lose value of their investment while residents lose jobs as businesses close but it also deters new investors from investing in the run-down cities. Therefore, 'starting from scratch' through charter cities has been canvassed as an alternative.¹⁵

In summary, the notion of charter city, as conceptualised by Paul Romer,¹⁶ is about developing new cities with new laws and institutions conducive for economic development. Under this concept, a willing developing country offers an uninhabitant land within its borders for the creation of a new city, which should be large enough for a city to thrive. It then adopts a broad legal framework – a charter or constitutive act – that creates the city, spelling out basic rights of the residents and responsibilities of the city government but then imports functional rules from a developed country/countries being guarantor(s), and the latter ensure(s) enforcement of these rules. The rules, which include institutions, are attractive to business and serve as incentive for the investors to set up industry in this new city. The city is autonomous from the host although it functions within a broad founding framework as adopted by the host. The inhabitants (residents and investors) have freedom of entry and exit. There is a source, being a country that provides people to populate the city.¹⁷ Once experienced and successful, there will be a domino effect of many new cities that are in a very good economic position thereby leading to overall development of the host country. Because of the difficulties in getting consensus to effect change at the national level, charter cities become a vehicle through which change can be effected at small scales until it becomes nation-wide.¹⁸

Against the above background, this paper, while endorsing charter cities, seeks to address some of the challenges towards effective implementation of charter cities for African countries.

¹⁴ Lael Bethlehem, 'A new dynamic – urban regeneration in the Joburg CBD,' 2013 *The Journal of the Helen Suzman Foundation* 69, 17-24.

¹⁵Paul Romer, Technologies, Rules, and Progress: The Case for Charter Cities (Center for Global Development Essay, 2010), available at: <u>file:///C:/Users/A0042183/Downloads/Document11242010360.9436609%20(1).pdf</u>, accessed 19 October 2021; Matt Coetzee, 'Charter Cities: What if we could start from scratch?' 2017 *Construction Research and Innovation* 8(4): 117-120.

¹⁶ Paul Romer, Technologies, Rules, and Progress: The Case for Charter Cities (Center for Global Development Essay, 2010), available at: <u>file:///C:/Users/A0042183/Downloads/Document11242010360.9436609%20(1).pdf</u>, accessed 15 October 2021.

¹⁷ Paul Romer, Technologies, Rules, and Progress: The Case for Charter Cities (Center for Global Development Essay, 2010), available at: <u>file:///C:/Users/A0042183/Downloads/Document11242010360.9436609%20(1).pdf</u>, accessed 15 October 2021; Brandon Fuller and Paul Romer, Success and the city: How charter cities could transform the developing world, (Macdonald-Laurier Institute, 2012).

¹⁸ Kee-Cheok Cheong, 'Charter Cities: An idea whose time has come or should have gone?' 2010 *Malaysian Journal of Economic* 47(2): 165-168.

Addressing conceptual problems for charter cities

Free uses of uninhabited land with proximity to sea

One of the salient features of charter cities is that they must be developed on an uninhabited land, probably outside the main cities and closer to sea for international trade. It may be hard to find uninhabited land where the city can be developed although not impossible. There is a proposal to relocate the inhabitants from an area that is earmarked for developing the charter city.¹⁹ While relocations have been carried out in other countries for economic growth, the challenge with developing countries is that relocations are not carried out in dignity of those who are being relocated. Thus, relocated people find themselves in precarious conditions as it happened in the Kingdom of Lesotho where residents of the areas surrounding one of the Lesotho Water Highlands Projects (Mohale Dam) were relocated to the capital city, Maseru. The relocated left behind their ways of livelihood – subsistence farming, and they were cramped in small plots where one could not have even one line of vegetables, thereby introducing poverty that was foreign to them.²⁰ In some countries in Africa, relocations for investment projects have been carried out through threats of violence and even massacres.²¹ Therefore, the language of relocations for charter cities brings horror in our minds and foreshadows any economic development that a charter city can bring. If at all, relocations must be done with dignity, taking into account cultural, socio-economic practices and the needs of the communities that are subject to relocations.

As indicated above, there is no doubt that charter cities can be an answer to African poverty and underdevelopment crisis; therefore, limiting the development of charter cities to proximity to sea for international trade would mean that only coastal countries would benefit from this model of economic development. Given that many African countries, as are many other countries in other continents, are landlocked, countries should rather adopt a radical mechanism for direct access to the sea beyond just the right of passage and transit as contained in The Convention on Transit Trade of Land-locked States or other instruments such as WTO Trade Facilitation Agreement.²² The corridor proposed here briefly entails designating physical space for a landlocked state to construct its rail or road passage to the sea, which does not require clearance at the border of the coastal state. The prevalence of non-tariff barriers in Africa indicates that despite

¹⁹ Voxi Heinrich Amavilah, 'Romer's Charter City v Colonization, Imperialism and Colonialism: A General Characterization,' (2011) *Resource and Engineering Economics Publications Services*, available at <u>https://mpra.ub.uni-</u> <u>muenchen.de/29974/1/MPRA_paper_29974.pdf</u>, accessed 17 October 2021.

²⁰ Motlatsi Thabane, 'Shifts from Old to New Social and Ecological Environments in the Lesotho Highlands Water Scheme; Relocating Residents of the Mohale Dam Area,' 2000 *Journal of Southern African Studies* 26(4): 633-654; Lenka Thamae, 'The Irony of Development: communities impacted by the Lesotho Highlands water Project,' available at: <u>https://www.protimos.org/uploads/6/6/2/1/6621888/the_irony_of_development_l_thamae.pdf</u>, accessed 18 October 2021.

²¹ 'Tendele's coal mine leaves local communities without water. It was denounced by the South African Human Rights Commission, WoMin, The Women's Water Assembly, for its human rights and environmental violations. Murder of local environmental activist,' available at: https://ejatlas.org/conflict/tendele-coal-mine-somkhele-kwazulu-natal

²² Ernesta Swanepoel, 'The Law of the Sea and Landlocked States,' Policy Briefing 205 (2020), available at: <u>https://media.africaportal.org/documents/Policy-Briefing-205-swanepoel_1.pdf</u>, accessed 20 October 2021.

the rights of land-locked countries, countries still face difficulties at the borders and this hinder flow of international trade.

Proponents of charter cities do not envisage investors to pay compensation to the host country for the use of the required uninhabited land. Indeed, there was no royalty or any form of rental fee for the use of large tracks of land that Madagascar had planned on leasing to Daewoo in pursuance of botched 'farming charter city'.²³ It is important to note that whereas the host desperately needs a vehicle for economic development, investors too are not running charity or providing aid to the developing country host; they are there for profit. Therefore, it is imperative for investors to pay for the use of land while enjoying the benefits of good rules and institutions. Otherwise, using resources freely may be seen as continuation of colonial tendencies where colonial masters exploited African resources without just compensation. Given shortages of agricultural land in many parts of the world,²⁴ if charters cities can be developed with free exploitation of Africa's precious resource – land, there can be influx of farming charter cities, which are not geared for economic development of the host but for agricultural export for purposes of food security at home instead of commercial export.²⁵ The only benefit that residents will gain would be low wages from the farms, with no potential for growth.

Governance

The most important aspect of charter cities is that they are autonomous or at least semi-autonomous from the host that created them although they do not have a status of a state. They are of course connected to the host to the extent that the former must act within the bounds of the constitutive act or charter that they are founded on. The city's undertakings cannot be subject to the authority of the host.²⁶ The residents enjoy basic civil rights such as equality before the law; however, political rights would be at bay from the city. This is because the city's governance is not derived from the ballot but from skills.

From the foregoing, charter cities are therefore criticised for being undemocratic. Specifically, the criticism is that charter cities entrench neo-liberal colonial ideas and Washington consensus where working class in poor countries are not seen as worthy to govern themselves and that the working class is subjected to the capital.²⁷ In response to this criticism, one needs to recall that the reason developing countries are in this dire state of

²³ Song Jung-a, Christian Oliver, and Tom Burgis, 'Daewoo to cultivate Madagascar land for free,' Financial Times (19 November 2008) available at: <u>https://www.ft.com/content/6e894c6a-b65c-11dd-89dd-0000779fd18c</u>, accessed 23 October 2021.

²⁴ <u>Ernest Aryeetey</u> and <u>Zenia Lewis</u>, 'African Land Grabbing: Whose Interests Are Served?' (2010), available at: <u>https://www.brookings.edu/articles/african-land-grabbing-whose-interests-are-served/</u>, accessed 22 October 2021.

²⁵ Lorenzo Cotula, Sonja Vermeulen, Rebeca Leonard and James Keeley, 'Land grab or development opportunity? Agricultural investment and international land deals in Africa,' (2009), available at: <u>https://www.fao.org/3/ak241e/ak241e.pdf</u>, accessed 28 October 2021.

²⁶ Rahul Sagar, 'Are Charter Cities Legitimate?' 2016 Journal of Political Philosophy 24(4), 509-529, 513.

²⁷ Rahul Sagar, 'Are Charter Cities Legitimate?' 2016 Journal of Political Philosophy 24(4), 509-529, 514.

poverty and underdevelopment is as a result of poor governance, archaic rules that are not supportive of business, and politics of self-interest. There is established literature that multi-party democracy might actually be a source of problems for African countries.²⁸

...Africa is not ready for democracy. Africans neither want it nor understand it. What Africa really needs is food, stability, and development. Democracy is just another fad – another Western imposition. Little has changed in Africa: the dictators are still in place, and corruption and human rights abuse are the norm. Democracy only leads to tribalism and war; it hinders economic development. Africa is still too poor and illiterate for democracy...All the foreign aid to Africa only makes the situation worse.²⁹

With the above quotation in mind, getting a system where popular democracy is eliminated and only those that can run the city based on efficacy and efficiency for an overall goal of human development is an ideal goal. In South Africa, there is a report that municipalities and indeed government are run by officials with no skills hence service delivery protests across the country,³⁰ and this happens across many countries in Africa. Officials are given jobs based on their political affiliation rather than skills, and this is a norm in Africa. Once the city has reached a particular stage of economic development, attained practices and culture that advances growth and development, and abandoned the old bad African ways, it can move to democracy. In fact, through charter cities, African countries can get a chance to start afresh and experiment with different forms of governance as other countries have – no country woke up into democracy, it has been a long journey into democracy yet African countries moved from colonialism to democracy and the results have been utter failure. In fact, democracy is not a panacea – legitimacy of regimes must be judged on their decency and aspiration to attain human development.³¹

In democracy, residents express their dissatisfaction by voting the current regime out. In charter cities, Romer advances that unsatisfied residents can always revolt against the city by exiting the city. The challenges of voting with feet have been addressed elsewhere by other scholars;³² I propose herein that the cities' residents can express their dissatisfaction through courts in which they would be challenging non-adherence to the agreed goals (social pact) between the governor of the city and the residents. This would ensure that only legitimate

²⁸ Ezeanyika S.Ezeanyika, 'Can Western Democracy Models be institutionalized in Africa? Reviewing Contemporary Problems and Prospects' 2011 *Ufahamu: A Journal of African* Studies, 36(2): 1-22; Maxwell Owusu, 'Democracy and Africa -- A View from the Village,' 1992 *The Journal of Modern African Studies* 30(3); 369-396, 380;

²⁹ Ezeanyika S Ezeanyika, 'Can Western Democracy Models be institutionalized in Africa? Reviewing Contemporary Problems and Prospects' 2011 *Ufahamu: A Journal of African* Studies, 36(2): 1-22, 13, quoting David L Peterson, 'Debunking Ten Myths about Democracy in Africa' 1994 *Washington Quarterly* 17(3): 129-141.

³⁰ 'Almost half of South Africa's senior municipal officials don't meet minimum competency levels' BusinessTech (12 April 2021), available at: <u>https://businesstech.co.za/news/government/483989/almost-half-of-south-africas-senior-municipal-officials-dont-meet-minimum-competency-levels/</u>, accessed 25 October 2021.

³¹ John Rawls, The Law of Peoples (Massachusetts: Harvard University Press, 2001) 85.

³² Rahul Sagar, 'Are Charter Cities Legitimate?' 2016 Journal of Political Philosophy 24(4), 509-529, 514.

goals are litigated rather than allowing populism and politics of special interest that have destroyed economies, and stifled much needed reforms.³³

One of the salient features of governance of charter cities is that a guarantor enforces the rules. Specifically, the status of guarantor is canvassed as being a developed country while the hosts are developing countries. The idea that guarantors can only be developed nations is flawed, and it ignores the fact that some developing countries can enforce the rules better than developed countries. In fact, for charter cities to gain legitimacy, and avoid criticisms of imperialism or supremacism, it has to be conceptually clear from the outset that charter cities are not only meant for developing countries although developing countries will mainly be the net beneficiaries given their levels of poverty and underdevelopment; however, developed nations can as well create charter citizens.³⁴ Therefore, hosts can also be developed countries because some developed nations have so much uneven economic development that they actually need charter cities to uplift the quality of life of their citizens in the neglected areas. As an example, COVID-19 exposed the US's troubles of poverty among some communities so much than the US should consider charter cities as well.³⁵ Regarding guarantors, it is argued herein that only countries that are stable, economically progressive and politically neutral at the international level can be guarantors. Thus, there can be a list, compiled by any of the Bretton Woods institutions, of stable and neutral countries as guarantors, and those can include countries such as Switzerland, Scandinavian countries, Canada, Australia, New Zealand, Botswana, Mauritius.³⁶ These are the countries, which command some high degree of respect among their peers given their neutrality, and their refrain from exercising their hegemony onto others.

The common criticism that charter cities are akin to colonization, imperialism and colonialism has been succinctly addressed elsewhere,³⁷ and will not be addressed here.

³³ Christopher Freiman, 'Cosmopolitanism within borders: On behalf of charter cities' (2013) Journal of Applied Philosophy 30(1), 40-54, 41.

³⁴ Matt Coetzee, 'Charter Cities: What if we could start from scratch?' 2017 Construction Research and Innovation 8(4): 117-120, 117. ³⁵Brea L. Perrya , Brian Aronsona and Bernice A. Pescosolido, 'Pandemic precarity: COVID-19 is exposing and exacerbating inequalities in the American heartland' (2020) Proceedings of the National Academy of Sciences and of the United States of America, available at: <u>https://www.pnas.org/content/118/8/e2020685118</u>, accessed 2 November 2021.

³⁶ In fact, had the charter city in Madagascar gone forward, Mauritius was going to be a guarantor administering export-processing zone, Kee-Cheok Cheong, 'Charter Cities: An idea whose time has come or should have gone?' 2010 *Malaysian Journal of Economic* 47(2): 165-168, 167.

³⁷ Voxi Heinrich Amavilah, 'Romer's Charter City v Colonization, Imperialism and Colonialism: A General Characterization,' (2011) Resource and Engineering Economics Publications Services, available at <u>https://mpra.ub.uni-</u> muenchen.de/29974/1/MPRA paper 29974.pdf, accessed 15 October 2021.

Exploitation

One of the main arguments against charter cities is exploitation of residents through dehumanising wages. Romer and Fuller envisage that in the immediate term, wages may not be huge as many jobs would be industrial.³⁸ Of course, charter cities will start off with low wages,³⁹ which is an incentive for the investor to consider setting up industry in the charter city. In fact, this is what developing countries use in their campaign to lure foreign investors – they talk of low or competitive wages. Low wages do not necessarily mean exploitation – it's all about the type of jobs and skills that are usually available in any given country in its development journey. This is the reason developing countries develop industrialisation policies – they aim at massive employment for unskilled citizens/residents. As this industry grows coupled with low political risk, other light industries can move into the city, and this will have domino effect on all other industries and wages will become high.⁴⁰ It is not long ago when American and European firms flocked to China for low wages yet today, there is exodus of firms exiting China because wages have become high – of course many still remain.⁴¹

Migration

Another key feature of Romer's charter cities is free movement of people, in which everyone who chooses to reside in the charter city can do so or exit whenever they want to. This is problematic to the extent that it opens up migration to everyone to the city, and it therefore cannot serve the purpose of the city, which is to uplift the residents of the host gradually until economic reforms are extended to the whole country. The proposal I make here is that residency should be open to the nationals of the host unless foreigners have skills that are in short supply in the city. Even nationals of the host should not just relocate to the new city without a job; residency must be contingent on the jobs otherwise jobless and homeless people can soon slum the new city thereby making it no different from the existing cities. These limitations to residency are not draconian; in fact, they are applicable in any polity that wants to avoid migration that will not enhance the country.

³⁸ Brandon Fuller and Paul Romer, Success and the city: How charter cities could transform the developing world, (Macdonald-Laurier Institute, 2012).

³⁹ Christopher Freiman, 'Cosmopolitanism within borders: On behalf of charter cities' (2013) *Journal of Applied Philosophy* 30(1), 40-54, 48.

⁴⁰ <u>Michael Castle-Miller</u>, The Governance Market: A New Vision for Paul Romer's Charter Cities Concept,' at 4, available at: <u>https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2458669</u>, accessed 7 November 2021.

⁴¹ Prince Ghosh, 'The Exodus Of Chinese Manufacturing: Shutting Down 'The World's Factory' Forbes (18 September 2020), available at: <u>https://www.forbes.com/sites/princeghosh/2020/09/18/the-exodus-of-chinese-manufacturing-shutting-down-the-worlds-factory/?sh=73ebdb44c2f2</u>, accessed 7 November 2021.

Conclusion

It is regrettable that charter cities in Honduras and Madagascar never took off; it is a missed opportunity for the international community to have experienced charter cities since Paul Romer made this proposal. Charter cities can enhance economic growth because they are insulated from bad laws, bad practices, inefficient and bad institutions.⁴²

It is has to be acknowledged that experimenting reforms and/or economic growth at large national scale is a risk that no individual country wants to experience as we have seen it with failed structural adjustments that were implemented at the national scale at the behest of International Monetary Fund and the World Bank. The situation is even volatile for developing countries that have not built their economies but inherited them from their colonial masters, thereby lacking knowledge and experience of how to build economies. In all developing African countries, new political parties are formed, old regimes are ousted yet economic challenges remain the same even with new administrations. These only point to well known problems – there are no skills, resources and political will to change dire economic situations in Africa. Consequently, the time is now for African economists, political scientists including lawyers to embrace the concept of charter cities, address inherent challenges and adapt it in a manner that will address African countries' needs, collectively and individually. There is a need to experiment at a smaller scale, in which we can get rid of special interest politics in the name of liberal democracy. We need to find land that can be used for this experiment – new city – while guarding against dehumanising relocations. City governors must have skills and vision for economic growth and human development. Migration into the city cannot be open to all as Africa is not a thoroughfare – international migrants must bring scarce skills otherwise we will be creating islands within Africa for expatriates.

⁴² Lan Cao, 'Charter Cities' 27(3) William and Mary Bill of Rights Journal, 717-764, 724.