31 STRATEGIES TO PROMOTE ECONOMIC GROWTH AND ECONOMIC DEVELOPMENT

REAL-WORLD ISSUE:
Why is economic development uneven?

By the end of this chapter, you should be able to:

Explain and evaluate the role of each of the following in achieving economic growth and development:

- Trade strategies, including import substitution, export promotion and economic integration
- Diversification
- Market based supply-side policies
- Foreign direct investment
- Social enterprise
- Redistribution policies
- Merit goods
- Institutional change
- Foreign aid, including official development assistance, non-governmental organisations and multilateral development assistance
- Debt relief.

In Chapter 30, we considered the barriers to economic growth and economic development. Now, we need to consider different strategies that might reduce or eliminate those barriers and enable developing countries to achieve economic progress. You must always be aware that economic growth is a one-dimensional concept relating only to an increase in real GDP. In contrast, economic development is a multidimensional concept relating to a myriad of improvements in well being. The importance of economic growth is not being questioned here. As noted in the Sustainable Development Goals, "Economic growth **can** lead to new and better employment opportunities and provide greater economic security for all"[1]. The word 'can' is key here. Economic growth will not contribute to economic development if the benefits of the growth are not shared equitably. Thus, the priority must be to achieve *inclusive growth* and adopt *'pro-poor' strategies* that directly confront the problem of poverty.

Economics in action — ATL Thinking, Communication and Research

In this section, we present a range of strategies, with just a few real-world examples, Therefore, for each strategy, it is expected that you will research your own real-world examples, so that you can come to your own conclusions about the strengths and limitations of the strategies in different contexts.

What strategies will enable the achievement of economic growth and/or economic development?

How can trade strategies be used to achieve economic growth and/or development?

International trade can undoubtedly contribute to economic growth and, when well-regulated, can definitely result in economic development. We look here at three different approaches that countries may adopt:

Key concept: INTERVENTION

1. **Import substitution**

   Import substitution is more fully known as import substitution industrialization (ISI). It may also be referred to as an inward-oriented strategy. It is a strategy that says that a developing country should, wherever possible, produce goods domestically, rather than import them. This should mean that the industries producing the goods domestically will be able to grow, as will the economy, and then the industries will be able to be competitive on world markets in the future, as they gain from economies of scale. It is the opposite of export-led growth and is not supported by those economists who believe in the advantages of free trade based on comparative advantage.

   In order for the strategy to work there are some necessary conditions:

   - The government needs to adopt a policy of organizing the selection of goods to produce domestically. Historically, this has been labour-intensive, low-skill manufactured goods, such as clothing or shoes.

[1] **Source:** United Nations Statistics Division, Goal 8, https://unstats.un.org/sdgs/report/2016/goal-08/

- Subsidies are made available to encourage domestic industries.
- The government needs to implement a protectionist system with tariff barriers to keep out foreign imports.

Investment projects for import substitution to be implemented in Kazakhstan

https://en.trend.az/business/economy/3109530.html

There are a number of perceived advantages and disadvantages with ISI:

Advantages

➔ ISI protects jobs in the domestic market, since foreign firms are prevented from competing, which means that domestic firms can dominate the market.

➔ ISI protects the local culture and social habits by practically isolating the economy from foreign influence.

➔ ISI protects the economy from the power, and possibly bad influence, of multinational corporations.

Disadvantages

➔ ISI may only protect jobs in the short run. In the long run, economic growth may be lower in the economy and the lack of growth may lead to a lack of job creation.

➔ ISI means that the country does not enjoy the benefits to be gained from comparative advantage and specialization, so producing products relatively inefficiently, when they could be imported from efficient foreign producers.

➔ ISI may lead to inefficiency in domestic industries, because competition is not there to encourage research and development.

➔ ISI may lead to high rates of inflation due to domestic aggregate supply constraints.

➔ ISI may cause other countries to take retaliatory protectionist measures.

The main countries to adopt ISI strategies were in Latin America, including Argentina, Brazil, Mexico, Chile and Uruguay. As former colonies gained their independence many also adopted inward-oriented strategies. These included India, Nigeria and Kenya. These policies showed some success in the 1960s and 1970s, but the policies started to fail in the early 1980s and were abandoned. At the present time, ISI does not seem to be a chosen option for economic growth.

2. **Export promotion**

Export promotion, often called export-led growth, is an outward-oriented growth strategy, based on openness and increased international trade. It is where growth is achieved by concentrating on increasing exports and export revenue as a leading factor in the aggregate demand of the country. Increasing exports should lead to increasing GDP and this in turn should lead to higher incomes and, eventually, growth in domestic and exporting markets. The country concentrates on producing and exporting products in which it has a comparative advantage of production. In addition, the country may attempt to 'manage' its exchange rate, keeping the rate as low as possible against other currencies and thus making its exports more attractive.

In order to achieve export-led growth, it is assumed that a country will need to adopt certain policies. These include:

- Liberalized trade: Open up domestic markets to foreign competition in order to gain access to foreign markets.
- Liberalized capital flows: Reduce restrictions on foreign direct investment.
- A floating exchange rate.
- Investment in the provision of infrastructure to enable trade to take place.
- Deregulation and minimal government intervention.

The list illustrates the theoretical "package" of policies associated with export-led growth. In reality, countries that adopt an outward-oriented strategy do not necessarily adopt all of these policies.

Developing countries may attempt to export either primary products and/or manufactured products (some have tried to export services, usually in the form of tourism). We should consider the differences involved in using the export of primary or manufactured products as the engine for growth.

- Many developing countries depend upon the export of primary products in order to gain export revenue. However, the overall trend in primary product prices, with the exception of oil and some metals, has been downward for many years. This is due to increasing supply and relatively insignificant increases in demand for many commodities. This, combined with increased protectionism by developed countries, means that export-led growth based on the export of primary products is unlikely to be achieved.
- The focus of export-led growth is usually on increasing manufacturing exports. The historic success of countries such as Japan, South Korea, Hong Kong, Singapore and Taiwan, known as the "Asian tigers", is usually used to illustrate the effectiveness of such a strategy. These countries exported products in which they had a comparative advantage, usually based upon low-cost labour, and were extremely successful in doing so. Over time, the type of product being exported by the majority of these countries has also tended to change from products that were produced using labour-intensive production methods, requiring low skill levels from the workers, to more sophisticated products, using capital-intensive production methods and more highly skilled workers. Improvements in education systems were essential for this.

Although it would appear that export-led growth is an obvious way to gain success, this is not necessarily the case. There are a number of problems associated with export-led growth:

- The success of the "Asian tigers", since around 1965, and the emergence of China as an exporting powerhouse, has led to increased protectionism in developed countries against manufactured products from developing countries. Trade unions and workers in developed countries argued that they could not compete against the imports from low-wage developing countries and that this was unfair. They lobbied their governments to put tariffs and quotas on the lower-priced goods. Price increases as a result of tariffs effectively removed the comparative advantage of the exporting countries. *Tariff escalation* also reduced the ability of the developing countries to export processed goods and assembled products, forcing many to export primary products and low-skilled manufactured goods instead.
- Certain assumptions were made about the necessary conditions for export-led growth. If we look at the successful countries, these conditions were not necessarily met. Many economists would argue that the role of the state in successful export-led growth is vital and that minimizing government intervention is not the way forward. In the "Asian tiger" countries, governments played an important role by providing infrastructure, subsidizing output through low credit terms via central banks, and promoting savings and improvements in technology. In addition, governments adopted policies where they protected domestic industries that were not yet able to compete with foreign firms and promoted the industries that were ready for competition in export markets. This illustrates the "infant industry" argument for protection. This topic is one of great debate amongst development economists and many argue that intervention is vital. Others argue that state intervention in these economies actually slowed down growth rates.
- If countries attempt to kick-start their export-led growth by attracting MNCs, there is always the fear that the MNCs may become too powerful within the country and that this may lead to problems.
- It is argued by some economists that free-market, export-led growth may increase income inequality in the country. If this is the case, then economic growth may be achieved at the expense of economic development.

Key concept
INTERVENTION

Nigeria eager to implement free continental trade agreement

https://www.africanews.com/2019/07/29/nigeria-eager-to-implement-free-continental-trade-agreement/

3. **Economic integration**

Over the past decades, developing countries have been involved in many preferential access schemes and regional free-trade agreements. Such agreements offer important opportunities for countries to achieve economic growth and development. However, there are also challenges. To a large extent, the opportunities and challenges depend on the extent of the integration. That is, whether the integration is simply preferential access for particular goods, a free-trade area, a customs union or a common market.

Possible advantages/opportunities associate with economic integration:

- Larger export markets, may allow producers to gain economies of scale.
- Larger markets may encourage diversification and reduce dependence on a narrow range of commodities.
- Integration is likely to encourage regional cooperation in areas such as infrastructure, including transport and telecommunications.
- For landlocked countries, regional integration may offer vital links to ports and other infrastructure networks in neighbouring countries.
- There should be further stimulus for inward foreign direct investment, as foreign companies will benefit from the larger market size.
- If there is free movement of labour, this provides opportunities for workers to work in other member countries, and send remittances home.
- If there is free movement of capital, integration provides opportunities for companies to invest in other member countries.
- There may be greater political stability and cooperation, which can result in higher levels of investment.
- Greater efficiency as domestic producers will have to compete with lower priced imports from other member countries.
- As part of a trading bloc, individual countries may increase their bargaining power in multilateral trade negotiations.
- Consumers may have access to less expensive imported goods and services. (However, this might be limited if trade diversion takes place and the new common external tariff makes some imported products more expensive **HL only**).
- Trade creation will benefit producers who can import inputs without tariffs (**HL only**).

Possible disadvantages/challenges associated with economic integration

- The role of the WTO might be undermined, since it allows member countries to look inwards.
- Trade can become more complicated with agreements with other trading blocs.
- Unemployment may arise, as less efficient companies (with higher labour costs), may not be able to compete with lower priced imports from other member countries.
- We may encounter trade diversion (**HL only**).

What is "aid-for-trade"?

In recognising the vast opportunities that trade offers in terms of growth **and** poverty reduction, the 2030 Agenda for Sustainable Development is calling for increasing "aid-for-trade" support for developing countries. The Aid for Trade initiative was launched in 2006 through the World Trade Organisation, and aims to provide:

- technical assistance to help countries negotiate trade strategies and implement outcomes of trade negotiations
- transport infrastructure to connect domestic and international markets and storage facilities
- support for agriculture, energy generation and supply
- investment in industries so that countries can diversify and build on comparative advantage
- adjustment assistance to help with the costs associated with tariff reductions and loss of preferential treatment.

Although there is no specific trade goal within the SDGs, there are around 20 targets in different SDGs that relate directly to international trade. Importantly, Target 8.A calls to "increase aid-for-trade support for developing countries, in particular least developed countries".

With such attention and international cooperation in expanding trade capacities and access to developing countries, it is hoped that trade will be a positive force for economic growth and poverty reduction.

Higher Level

Higher Level

Economics in action — ATL Thinking, Communication and Research

There are many examples of regional economic integration (trade blocs) among developing countries. Find an example and identify the challenges and opportunities that membership in the bloc brings to its members. How might "aid-for-trade" help to overcome the challenges?

How might diversification of economic activity help to achieve economic growth and/or development?

As we have already discovered, one major problem for a number of developing countries has been over-dependence upon exporting a limited range of primary commodities. In many cases countries have been dependent upon export earnings from one, or possibly two, commodities.

The Advancing Economic Diversification in Ethiopia Project launches

https://www.africanews.com/2019/08/23/launch-of-the-advancing-economic-diversification-in-ethiopia-project/

Many countries are now pursuing export diversification as a means to gain economic growth. The aim is to move from the production and export of primary commodities and to replace these with the production and export of manufactured and semi-manufactured products. In doing this they hope to protect themselves from the volatile changes in primary product prices, to stabilize or increase export revenue and to stabilize or increase employment. There will also be an increased use of technology and an increased demand for more highly skilled workers.

There are a number of barriers to the strategy of diversification. One is the practice of tariff escalation, whereby the rate of import tariffs on goods rises the more the goods are processed. So, the importing country protects its processing and manufacturing industries by putting lower tariffs on imports of raw materials and components and higher tariffs on processed and finished products. There is little incentive for developing countries to diversify away from producing raw materials to processing them, as the higher prices caused by the tariffs will make their processed goods uncompetitive.

A second barrier is the need for a more highly qualified workforce in order to produce relatively more sophisticated products. As we already know, many developing countries have relatively low educational standards and find it difficult to fund an improving educational system. If this is the case, then the country is in a poverty trap. Low education leads to the production of low profit commodities and components, which leads to low incomes for governments and individuals, which perpetuates the low ability to fund education.

How can market-based supply-side policies impact economic growth and/or development?

There are three market-based supply-side policies that are most often put forward as a means of achieving economic growth. These are:

1. **Trade liberalization**

   Trade liberalization is the removal, or at least reduction, of trade barriers that block the free trade of goods and services between countries. It involves the elimination of such things as tariff barriers, quotas, export subsidies and administrative legislation.

   The belief is that trade liberalization will increase world trade and will enable developing countries to concentrate on the production of goods and services in which they have a comparative advantage. The advantages of free trade are covered in Chapter 23.

   However, many developing countries and in particular, the least developed countries, lack the infrastructure and institutions that are necessary to gain the full benefits from trade liberalization. In addition, protectionist policies employed by developed countries to block developing countries from exporting higher-value manufactured goods can reduce the effectiveness of trade liberalization for developing countries. Subsidies given by developed country governments to their producers can also damage the ability of producers from developing countries to compete in international markets.

   The challenges that developing countries face in terms of benefiting from trade liberalisation underscore the need for international cooperation through aid-for-trade strategies.

Key concept
EFFICIENCY

2. **Privatization**

   This is the sale of public government-owned firms (nationalized firms) to the private sector. It is argued by free market economists that privately-owned, profit-maximizing firms will be more efficient than nationalized firms and will therefore increase the potential output of the economy. Nationalized firms tend to have different goals from private firms, such as maintenance of employment or the provision of a service to an isolated market, and this means that they may operate inefficiently.

   However, privatization will only generate economic gains if the process is carried out and managed well. The process of privatization requires careful design and sequencing, the creation of a regulatory infrastructure, assessment of possible poverty and social impacts, and transparent public communication. This is often challenging in developing countries.

   Furthermore, it may be necessary for some goods and services to be provided by nationalized firms in order that they be accessible and

Key concept
EFFICIENCY

affordable to everyone, particularly low income people. Should such industries be privatized, the result might be that certain operations are closed down because they are not profit-marking, or the price of the product might become unaffordable.

Civil society fights Jakarta water privatization during Annual Meetings in Bali

https://www.brettonwoodsproject.org/2018/09/civil-society-fights-jakarta-water-privatisation-annual-meetings-bali/

Consider the case of the provision of water and sanitation. Access to safe and affordable drinking water and sanitation is seen as a human right, and is an essential feature of any fight against poverty. Given the huge expense of providing such infrastructure, governments in developing countries have often turned to the private sector. Indeed, in some examples, governments were required to privatize such sectors in order to receive support from international agencies. Given that private companies have the financial resources to undertake the large investments necessary for such infrastructure projects, it is not difficult to see why privatization is an appealing option for cash-strapped governments. However, left purely to market forces, a lack of competition and regulation in the water industry means that the development goal of increased access to water at affordable prices is unlikely to be met. Therefore, if such an industry is to be privatized, it is necessary that the government is involved in establishing and enforcing regulations to ensure that the goal of providing safe and affordable water is reached.

3. **Deregulation**

As we know from Chapter 15, if governments have placed many regulations on the operations of businesses then this may increase their costs of production, thereby reducing potential output in the economy. Such regulations include environmental laws, health and safety regulations or laws concerning working hours, leave and holidays. A reduction in the number and/or the severity of regulations, ie deregulation, will help to increase aggregate supply and thus generate economic growth.

Key concept

EFFICIENCY

In many developing countries, there is much 'red tape' involved when starting up a business and, if this is the case, then it will deter both domestic and foreign investors. Reducing the difficulty of the process may well increase investment.

The World Bank *Ease of Doing Business Index* measures how simple it is to conduct business in a country. The ease of doing business score measures the gap between an economy's performance and a measure of best practice across 41 indicators for 10 Doing Business topics. The topics considered are Starting a business; Dealing with construction permits; Getting electricity; Registering property; Getting credit; Protecting minority investors; Paying taxes; Trading across borders; Enforcing contracts; and Resolving insolvency. Table 31.1 shows a selection of figures for 2018 and 2019.

Country (DB rank)	Doing business score 2018	Doing business score 2019
New Zealand (1)	86.6	86.6
Singapore (2)	85.0	85.2
Denmark (3)	84.0	84.6
South Sudan (185)	33.3	35.3
Libya (186)	33.2	33.4
Yemen (187)	33.0	32.4
Venezuela (188)	30.9	30.6
Eritrea (189)	22.9	23.0
Somalia (190)	20.0	20.0

Source: *Doing Business*, The World Bank, 2019 http://www.doingbusiness.org

▲ **Table 31.1** Doing Business Index scores for top and bottom countries, 2018 & 2019

However, it should be remembered that deregulation does have its drawbacks and detractors. If the deregulation of labour laws to attract investment damages the safety and rights of workers, then any benefits in terms of economic growth will not be inclusive. In the same way, if deregulation of the banking system leads to debt-driven growth as opposed to growth through industrial development and infrastructural change, then again, there will be growth at the cost of development. Lastly, if deregulation relates to the relaxing of environmental laws, then any growth will be at the cost of sustainable development.

How can foreign direct investment impact economic growth and/or economic development?

Foreign direct investment (FDI) is long-term investment by private multinational enterprises/corporations (MNEs or MNCs) in countries overseas. FDI usually occurs in one of two ways. MNCs either build new plants or expand their existing facilities in foreign countries (is known as greenfield investment) or MNCs merge with or acquire (buy) existing firms in foreign countries.

MNCs are attracted to developing countries for a number of reasons:

- The countries may be rich in natural resources, such as oil and minerals. MNCs have the technology and expertise to extract such resources. For example, among the top recipients of FDI in Africa are those countries with valuable natural resources, such as Nigeria and South Africa.
- Some developing countries, such as Brazil, China and India, represent huge and growing markets. If MNCs are located directly in the markets then they have much better access to the large

number of potential consumers. With growing incomes, demand for all sorts of consumer goods is rising and MNCs wish to be there to satisfy the demand.

- The costs of labour are much lower than in more developed countries. Lower costs of production allow firms to sell their final products at lower prices and make higher profits.
- In many developing countries government regulations are much less severe than those in developed countries. This makes it easier for companies to set up but, more significantly, it can greatly reduce costs of production. Additionally, many developing country governments offer tax concessions to attract foreign direct investment. Over the last fifteen years many countries, both developed and developing, have adopted policies that have been more and more favourable to foreign direct investment. This often takes the form of reducing corporate tax rates.

We should now consider the possible advantages and disadvantages that may arise for developing countries from receiving FDI from MNCs:

Key concept
EFFICIENCY

Possible advantages associated with FDI are:

- As we know from macroeconomics, a necessary condition for growth is increased savings and developing countries tend to suffer from a *savings gap*. FDI helps to fill that savings gap and thus may lead to economic growth.
- MNCs will provide employment in the country and, in many cases, may also provide education and training. This may improve the skill levels of the work force and also the managerial capabilities.
- MNCs allow developing countries greater access to research and development, technology and marketing expertise and these can enhance their industrialization.
- Increased employment and earnings may have a multiplier effect on the host economy, stimulating growth.
- The host government may gain tax revenue from the profits of the MNC, which can then be used to gain more growth by investing in infrastructure, or to improve public services, such as health and education, to promote economic development.
- If MNCs buy existing companies in developing countries, then they are injecting foreign capital and increasing the aggregate demand.
- In some cases, MNCs may improve the infrastructure of the economy, both physical and financial, or they may act as a spur for governments to do so, in order to attract them.
- The existence of MNCs in a country may provide more choice and lower prices for consumers. They may be able to provide essential goods that are not available domestically.
- MNC activities along with liberalized trade can lead to a more efficient allocation of world resources.

It is clear that there are vast gains to be made from FDI. This can be clearly shown using China as an example. Although it is difficult to isolate FDI in terms of its effect on China's economic growth, it is reasonable to assume that it has played a significant role. Since 1978, China has actively tried to attract foreign investment as a way to stimulate economic growth. A significant proportion of China's exports are produced by foreign firms. Through joint ventures with foreign firms, Chinese firms have grown rapidly and successfully and China itself is now the source of a large outflow of foreign direct investment. As China grows, so does its demand for raw materials and much of Chinese FDI abroad is its investment in natural resources.

Possible disadvantages associated with FDI are:

- Although MNCs do provide employment, it is argued that they often bring in their own management teams, simply using inexpensive low skilled workers for basic production, and providing no education or training. This also limits the ability of host countries to acquire new technologies.
- In some cases it is argued that MNCs have too much power, because of their size, and so gain large tax advantages or even subsidies, reducing potential government income in developing countries. Along the same lines, it is argued that MNCs have too much power internationally. Their incomes and size allow them to exert too much influence on policy decisions taken in institutions such as the WTO.
- MNCs practise transfer pricing, where they sell goods and services from one division of the company to another division of the company in a separate country, in order to take advantage of different tax rates on corporate profits. In this way, developing countries with low tax rates to encourage MNCs to invest, reap little tax reward and developed countries also lose out on potential tax revenue. Given that approximately one-third of all international trade is made up of sales from one branch of a firm to another firm, this represents a potentially large loss of revenue to governments. Governments have rules to prevent firms from abusing their ability to use transfer pricing to minimize their tax payments, but these are difficult to monitor and enforce, particularly for developing country governments.
- It is argued that MNCs situate themselves in countries where legislation on pollution is not effective and thus they are able to reduce their private costs while creating external costs. Whilst this is good for the MNC it is obviously damaging for the environment of the host country. In the same way MNCs may set up in countries where labour laws are weak allowing the exploitation of local workers in terms of both low wage levels and poor working conditions.
- It is argued that MNCs may enter a country in order to extract particular resources, such as metals or stones, then strip those

Key concept
SUSTAINABILITY

Key concept
EQUITY

resources and leave. There may be significant unrest as host country nationals see that the profits from their resources are being sent out of the country to foreigners.

- Economists have argued that MNCs may use capital-intensive production methods to make use of abundant natural resources. This will not greatly improve levels of employment in the country. It is argued that the MNCs should use appropriate technology, where production methods are aligned to the resources available. Since developing countries usually have a large supply of cheap labour, the argument is that labour-intensive production methods would be more appropriate.
- In most cases, where MNCs buy domestic firms, the owners of the firms being bought are paid in shares (stocks) from the MNC. This means that it is likely that the actual money will never be used in the developing country's economy.
- MNCs may repatriate their profits, which means that they transfer their profits out of the country back to the MNC's country of origin.

Uganda is surrendering trillions in tax agreements to multinational firms

https://www.monitor.co.ug/Business/Prosper/Uganda-trillions-tax-agreements-multinational-firms-/688616-5232786-77d0njz/index.html

Whilst most would agree that FDI is a positive factor for current economic growth, the main concerns relate to the possible negative effects of MNCs on sustainable economic development. The extent to which FDI is able to contribute to this development very much depends on the type of investment and the ability of the host country governments to appropriately regulate the behaviour of the MNCs and use the benefits of the investment to achieve development objectives.

To address some of the the concerns, the OECD *Guidelines for Multinational Enterprises*, provides a very detailed and extensive list of guidelines to all multinationals operating in, or coming from, any of the 48 countries that adhere to the Guidelines. The Guidelines provide "non-binding principles and standards for responsible business conduct in a global context, consistent with application laws and internationally recognised standards. They are the only multilaterally agreed and comprehensive code of responsible business conduct that governments have committed to promoting,"[2] Each member country has an agency serving as a National Contact Point (NCP) to promote and implement the Guidelines. These agencies also serve as a mediator for resolving issues.

Included in the many guidelines are the expectations that MNEs should:

- contribute to the economic, environmental and social progress with a view to achieving sustainable development
- respect internationally recognized human rights

[2] OECD Guidelines for Multinational Enterprises, 2011, http://www.oecd.org/daf/inv/mne/48004323.pdf\

- encourage local capacity building
- encourage human capital formation through providing employment and training opportunities
- provide full financial and operating information.

There have always been concerns related to MNC activity, such as the possible exploitation of workers, the use of child labour, the inability of workers to form trade unions, and business practices that cause immediate or future environmental damage. With the increasingly fast flow of information through the media and the internet and strong public interest groups acting globally, it is becoming difficult for MNCs to conceal activities that may contribute to these problems. They do not want to be perceived as being a cause of problems and are keen to promote their image in positive ways. As a result, firms are more and more likely to develop and publicize a set of policies to show that they are acting responsibly and ethically and "doing their bit" to promote sustainable development. As discussed earlier in this companion, this is known as Corporate Social Responsibility (CSR). Companies publish and promote their CSR policies through their annual reports, websites and advertising. The policies outline the firm's commitment to support human rights, employee rights, environmental protection, sustainable development and community involvement. The extent to which such policies are consistently followed and the extent of their actual effect on workers, the workers' communities and the environment is uncertain, but it is usually regarded as a step in the right direction!

Key concept

ECONOMIC WELLBEING

Did you know?

FDI remains the largest external source of finance for developing economies. FDI makes up 39 per cent of total incoming finance in developing economies as a group, but less than a quarter in the LDCs, with a declining trend since 2012.

→ FDI flows to developing economies remained stable in 2017 at $671 billion, seeing no recovery following the 10 per cent drop in 2016.

→ FDI flows to Africa continued to slide, reaching $42 billion, down 21 per cent from 2016. The decline was concentrated in the larger commodity exporters.

→ Flows to developing Asia remained stable, at $476 billion. The region regained its position as the largest FDI recipient in the world.

→ FDI to Latin America and the Caribbean rose 8 per cent to reach $151 billion, lifted by that region's economic recovery. This was the first rise in six years, but inflows remain well below the 2011 peak during the commodities boom.

→ FDI in structurally weak and vulnerable economies remained fragile. Flows to the least developed countries fell by 17 per cent, to $26 billion. Those to landlocked developing countries increased moderately, by 3 per cent, to $23 billion. Small island developing states saw their inflows increase by 4 per cent, to $4.1 billion.

Source: UNCTAD World Investment Report 2018

Economics in action

ATL Thinking, Communication and Research

Research and write a brief report explaining the CSR policies of any multinational company with respect to its work in a developing country. This is easily done by going to the homepage of the company. How does the company seem to be adhering to the OECD Guidelines that MNEs should "contribute to the economic, environmental and social progress with a view to achieving sustainable development"?

Warning – you will obviously be getting a one-sided view of their efforts!

Key concept
SUSTAINABILITY

Key concept
EQUITY

Key concept
EFFICIENCY

Key concept
CHANGE

How might social enterprise promote economic development?

Social enterprises are organizations that have specific social objectives as their primary goal. They may be for-profit, or non-profit organizations, but profit is a secondary goal. Most social enterprises aim for the creation of social wealth, a viable business model and environmentally responsible operation.

The principal objective and purpose of a social enterprise is to overcome, or alleviate, a global or local issue, such as poverty, a lack of education, a lack of health care, technology access or an environmental problem. However, as with any other business, the financial figures and cash flow must be capable of providing a sustainable, long-term existence. In addition, social enterprises are both gender sensitive and environmentally conscious.

A good example of a social enterprise is Sunny Money, an enterprise that aims to provide solar powered products to rural and off-grid communities in Africa. They produce a number of products, such as solar torches, solar lights and solar battery chargers, which they sell at very low prices. The selling is done through agents and so the businesses also create employment in the areas where they sell.

Some would argue that giving away the products would be better, ie providing them through a charity. However, the managing director of Sunny Money argues that "We have taken a market-based approach because we believe that only by helping to create a viable market, which serves the needs of customers, will any intervention be sustainable. Giving away products runs the risk of destroying a market which responds to the needs of the people. How can an entrepreneur in Kenya, for example, make a living out of selling solar lights if a nearby NGO is busy giving them away for free?"[3]

[3] **Source:** Adapted from *African social enterprises pave the way for solar power while stimulating the local economy,* May 2019, www.theguardian.com

The managing director is referring to the wider impact social enterprises are hoping to have. They don't only plan to provide affordable lighting, they also want to provide economic opportunities and help local entrepreneurs carve out their own successful solar power businesses.

Economics in action ATL Thinking, Communication and Research

Go to the website of Solar Sister: solarsister.org.

1. Identify the products that the enterprise offers.
2. Identify the social aims of the enterprise.
3. Explain the distribution system that the enterprise uses.
4. Explain the environmental elements of the operation.
5. Explain the different positive effects on development and sustainable development that are likely to be created by the activities of this enterprise.

Another valuable exercise would be to find your own example of a social enterprise working in a developing country, and explain its aims and achievements.

How can institutional change impact economic growth and/or economic development?

Key concept
CHANGE

We have already discovered that countries face certain institutional barriers to growth and development. It therefore follows that if the institutional framework can be reformed, then development is more likely. While there are a great many that could be investigated, we will consider three strategies that might promote favourable institutional changes:

1. **Improved access to the banking system**

   Developing countries face enormous challenges as a result of their weak financial systems. Anything that improves the access of individuals to the banking system will help with both growth and development. Two billion people worldwide still lack access to regulated financial services. Financial access and the underlying financial infrastructure taken for granted in rich countries, such as savings accounts, debit cards or credit as well as the payment systems on which they operate, still aren't available to many people in developing countries. This limits the ability of households and businesses to save, it affects the ability of people to buy and sell goods and services and very importantly, it limits the ability of entrepreneurs and firms to gain credit to start and expand businesses.

We will look at two areas of possible improvement:

- *Microfinance* – There is a type of financial service that is geared specifically to the poor. This is known as micro-finance and is the provision of financial services, such as small loans, savings accounts, insurance and even cheque books.

  The provision of small loans to individuals who have no access to traditional sources is known as micro-credit. A key element of original micro-credit schemes is that they did not originate in the developed world, but rather had their beginnings in developing countries. The first schemes began in the mid-1970s with projects such as Opportunity International (1972), ACCION International (1973), Muhammad Yunus/Grameen Bank (1974/76), FINCA International (inc 1985) and The SEEP Network (1985).

Africa's biggest bank is going after the continent's informal markets

https://qz.com/africa/1696196/standard-bank-signs-deal-with-nomanini-to-reach-informal-traders/

  Usually, the micro-credit loans are given to enable poor people to start up very small-scale businesses, known as micro-enterprises. These may include such things as roadside kiosks, bicycle repair services, market stalls, rice wine making, knitting and woodworking. The loans give protection against unexpected occurrences and seasonal problems, and may help families to gain a regular income, start to build wealth and thus escape from poverty.

  Women have tended to be the main recipients of micro-credit, for many reasons. It is thought that women are a better credit risk – they are more likely to pay back loans. Women are usually responsible for caring for children and so any reductions in a woman's poverty will translate into improvements for the children. In many documented cases, this has allowed for more poor children to go to school. When women take loans and can begin to earn an income, their social and economic status is raised and economic development is enhanced.

- *Mobile phone banking* – Access to banking services has been increased in recent times in developing countries with the advent of mobile phone banking and mobile money. In mobile banking a person who wants to send money does so by sending the amount via text to the receiver's phone number. The person who receives the money goes to an authorized local shop and withdraws the cash.

  Many mobile phone companies are taking over banking services in less developed countries. Africa is known as the "unbanked continent". Mobile banking is changing this. In Kenya and Tanzania, British operator *Vodafone* has over 33 million customers who send money to other people in the country and abroad via their M-Pesa system. Formal financial inclusion in Tanzania has increased from 44 percent in 2009 to over 65 percent at the present time.

  In Pakistan, Norwegian mobile phone company *Telenor* has been offering mobile banking since 2008. They have over 40 million subscribers. People can withdraw money at over 11,000 shops throughout the country. Pakistan itself has only 8,000 banks.

There are countless examples where mobile banking has contributed to development. For example, hospitals in Tanzania send money to women so that they can pay for the bus fare to the hospital. In Afghanistan the government pays its policemen by mobile phone. Coffee plantation owners in East Africa send workers their money via text. People who work in other countries, can much more easily, cost-effectively and securely send remittances home by using mobile bank services.

2. **Increasing women's empowerment**

Empowerment is the process by which women gain power and control over their own lives and acquire the ability to make strategic choices. As we discovered in Chapter 30, there are important externalities that occur when women become more empowered.

"Providing women and girls with equal access to education, health care, decent work and representation in political and economic decision-making processes will fuel sustainable economies and benefit societies and humanity at large. Implementing new legal frameworks regarding female equality in the workplace and the eradication of harmful practices targeted at women is crucial to ending the gender-based discrimination prevalent in many countries around the world"[4].

A strategy for women's empowerment should include:

- increasing support for the education of females
- increasing access to healthcare for women
- creating a safe environment in the home, the workplace and society
- establishing the right for women to own property and other assets
- increasing female involvement in decision making, both within the home and outside of it.

Economics in action ATL Thinking, Communication and Research

Go to the United Nations Development Program (UNDP) website: www.undp.org.

1. Find Goal 5, gender equality by clicking on the Goal 5 icon.
2. Make a note of the facts and figures offered.
3. View the Goal 5 targets.
4. Evaluate the success of your own country, or a country of your choice, in achieving the Goal 5 targets

[4] **Source:** SDG Goal 5, Gender equality, United Nations, www.un.org/sustainabledevelopment/gender-equality/

Exercise 31.1

ATL Thinking and Communication

Read the following article and summarize the benefits of women's empowerment in terms of climate change.

Education and family planning as tools to fight climate change

In 2017, an international coalition of well-known researchers, scientists and policy makers collaborated to offer a comprehensive set of 80 solutions to climate change in their book, *Drawdown, The Most Comprehensive Plan Ever Proposed to Reduce Global Warming*.

All of the solutions are economically viable, and all of them are already being used in various communities around the world. The challenge is to raise the profile of these solutions in order to slow down the earth's warming and reach 'drawdown', the point where the level of greenhouse gases in the atmosphere hit a peak and begin to fall, thus reversing global heating.

Many of the recommendations are well-known to us, and commonly recommended ways to reduce carbon emissions. The list below present the top ten. (You might have to look up 'silvopasture'!)

1	Refrigerant management
2	Wind turbines (onshore)
3	Reduced food waste
4	Plant-rich diet
5	Tropical forests
6	Educating girls
7	Family planning
8	Solar farms
9	Silvopasture
10	Rooftop solar

Two less well-known solutions are on the list at numbers 6 and 7 – the education of girls and family planning.

Let's look at Recommendation Number 6. The link between the education of girls and a smaller carbon footprint isn't as intuitively obvious as many of the others. However, there is ample evidence to support it. It's clear that if more girls go to school and get a quality education, the social benefits are profound: reduced incidence of disease, increased knowledge of nutrition, better employment opportunities, fewer forced marriages,

better job opportunities, higher life expectancies, and fewer children. Better educational access and attainment not only equips women with the skills to deal with the effects of climate change, but it empowers them to work with their communities to mitigate against it. Yet the education of girls lags far behind the education of boys in so many countries as both poverty and culture or tradition continue to mean that boys' education is prioritised.

Raising girls' education levels leads to Recommendation Number. 7 – access to family planning. The planet is overpopulated, and the demands of its citizens greatly exceed the natural resources provided by our environment.

Contraception and prenatal care is unavailable to women across the world, including developed and developing countries. It's either not available, not affordable, or social and/or religious motives mean that it's banned or heavily restricted. Without increasing awareness of, and granting access to family planning, the world's population will rise rapidly, consume ever more resources and require more and more energy to fuel its demands for goods and services. Carbon dioxide will continue to accumulate in the atmosphere.

In *Drawdown*, the authors calculated that the empowerment of women through educating girls and providing them access to family planning, would slow down the growth of the world's population and could lead to a reduction of 120 billion tons of emissions by 2050. This would be equivalent to 10 years' worth of China's annual emissions as of 2014.

Source: Adapted from The Wired, "To stop climate change, educate girls and give them birth control", https://www.wired.com/story/to-stop-climate-change-educate-girls-and-give-them-birth-control/

Key concept

EQUITY

3. **Reducing corruption**

We have already seen in Chapter 30 that corruption is a significant barrier to development. There is not a country in the world, developed or developing, that is immune to corruption. The abuse of public office for personal gain destroys people's trust in government and institutions, makes public policies less effective and fair, and takes taxpayers' money away from merit goods and public goods, such as schools, roads and hospitals.

Corruption limits the government's ability to help grow the economy in a way that benefits all citizens. As a result of corruption, governments receive lower tax revenue, because people pay bribes to avoid paying taxes. In addition, if people believe that the government itself is corrupt, then they will try to avoid paying taxes, since they know that the money will be misspent. In a recent IMF report, it was estimated that least corrupt governments can collect 4 percent more of GDP than similar countries with higher levels of corruption. For some countries, anti-corruption reforms have generated even higher GDP increases. For example, in Georgia, corruption was reduced significantly and tax revenues more than doubled, rising by 13 percentage points of GDP between 2003 and 2008. Reforms in Rwanda to fight corruption, since the mid-1990s, were successful, and tax revenues increased by 6 percentage points of GDP.[5]

Fighting corruption requires political will to create strong fiscal institutions that promote integrity, transparency and accountability throughout the public sector. The IMF suggest a number of measures that would help to reduce corruption:

- *Invest in high levels of transparency and independent external scrutiny.* This allows audit agencies and the public at large to provide effective oversight. For example, Colombia, Costa Rica and Paraguay are using an online platform that allows citizens to monitor the physical and financial progress of investment projects.
- *Reform institutions.* The chances for success are greater when countries design reforms to tackle corruption from all angles. For example, reforms to tax administration will have a greater payoff if tax laws are simpler and they reduce officials' scope for discretion.
- *Build a professional civil service.* Transparent, merit-based hiring and merit-based pay reduce the opportunities for corruption. The heads of agencies, ministries and public enterprises must promote ethical behavior by setting a clear tone at the top.
- *Keep pace with new challenges as technology and opportunities for wrongdoing evolve.* Focus on areas of higher risk – such as

[5] **Source:** Fiscal Monitor, International Monetary Fund, April 2019

procurement, revenue administration and management of natural resources – as well as effective internal controls. In Chile and Korea, for example, electronic procurement systems have been powerful tools to curtail corruption by promoting transparency and improving competition.

- *More cooperation to fight corruption.* Countries can join efforts to make it harder for corruption to cross borders. Countries can also aggressively pursue anti–money laundering activities and reduce transnational opportunities to hide corrupt money in opaque financial centers.[6]

We have already seen that corruption disproportionately affects vulnerable populations, the poor in general and women in particular. Corruption presents a particular barrier for women to gain full access to their civic, social and economic rights.

TRANSPARENCY INTERNATIONAL

▲ The logo of Transparency International

Transparency International have suggested several ways that countries could reduce the problem of gender and corruption:

- *Collect, analyse and disseminate gender desegregated data.* Timely access to sufficient, accurate and up-to-date information is essential in order to design, implement and monitor effective public policies and to better integrate gender into anti-corruption policies.
- *Recognize and address specific gendered forms of corruption.* Sexual extortion (sextortion), a form of corruption where sex is the currency of the bribe, is only one form of corruption that disproportionately affects women. Other forms of abusive behaviour are not always recognized as corruption and are less likely to be reported due to a culture of shaming and victim blaming. Countries should ensure their judicial systems have the necessary tools and awareness to address sextortion cases.
- *Include women in anti-corruption decision making.* To ensure fairer access to political rights, women have to be part of the formulation, implementation, monitoring and evaluation of anti-corruption policies.
- *Empower women.* Women are less likely to report abuse, as they are often unaware of their rights and entitlements, which makes them easier targets for corruption. Governments, international organizations, businesses and civil society organizations can and should play a key role to help ensure women have full knowledge of their rights through campaigns and information on gendered forms of corruption.
- *Gender sensitive reporting mechanisms.* Safe, accountable, accessible and, most importantly, gender sensitive mechanisms should be created to report corruption. These mechanisms

[6] **Source:** Adapted from *Tackling corruption in government*, by Vitor Gaspar, Paolo Mauro and Paulo Medas, April 4 2019, IMF, blogs.imf.org

should take into account cultural context and gender issues that might hinder reporting.[7]

4. **Promoting secure property rights and land tenure rights**

The prize-winning Peruvian economist Hernando de Soto divides the world into two groups: the ones who have defined property rights and those who do not. About two billion people have full rights to the property they live in and the land they farm, according to de Soto. For the 5.3 billion who do not have such rights, the implications are bleak: people are unable to use their resources to create wealth, and their assets become "dead capital" which cannot be used to generate income or growth. He argues that the poor are trapped by the "tragedy of the commons" that we looked at in Chapter 9. Because they don't own their property or land, their unregistered assets can effectively be stolen by more powerful entities.

It is often the case that poor people have the ability to use land for subsistence agriculture, or for grazing or for gathering firewood, but they lack the statutory, or legal right to determine its use, sell it, use it for collateral or leave it to their children. De Soto argues that legally protected property rights are the key source of the developed world's wealth and prosperity, and the lack thereof is the reason why many nations remain trapped in poverty. He estimates that providing the world's poor with titles for their land, homes and unregistered businesses would unlock $9.3 trillion in assets, an enormous sum to reduce poverty. Reforming legal structures to ensure property titles would allow the poor to use their small homes or land in order to borrow money and start businesses.[8]

The World Bank and other development organisations such as Oxfam, the International Development Law Organisation (IDLO) and the Food and Agricultural Organisation (FAO) work to raise awareness and improve the rights of people to own property and secure land tenure rights. The World Bank notes that there are seven key reasons why legal reforms to improve property and land rights are necessary for economic growth and development:[9]

1. **Secure land rights are an important pillar for agriculture**

   When farmers have secure land titles and know that their land rights will be guaranteed, they have the incentive to invest in their land and borrow money for agricultural inputs or to make improvements to the land.

Key concept
EQUITY

Key concept
CHANGE

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7 **Source:** Adapted from *Gender and corruption: where do we go from here?*, by M Amelia Berazategui, March 20 2019, Transparency International, voices.transparency.org

8 **Source:** *The Mystery of Capital*, by Hernando de Soto, 2003, Black Swan

9 **Source:** 7 reasons for land and property rights to be at the top of the global agenda. The World Bank Group, March 2019. https://blogs.worldbank.org/voices/7-reasons-land-and-property-rights-be-top-global-agenda

2. **Secure land rights are essential for urban development.**

   The formation of large informal settlements or slums in many cities is the result of a failure to clarify land rights. In order to create affordable and livable urban areas, effective urban planning is needed, but this is impossible without guaranteed land rights.

3. **Secure property rights help protect the environment.**

   When property rights are secure, people have far more incentive to look after their land, and ensure its sustainability.

4. **Secure property rights and access to land are crucial for private sector development and job creation.**

   The private sector needs land to build factories, commercial buildings and residential properties. Land or property rights give collateral to companies to help them finance their operations, expand their business or open new businesses, thus creating more jobs.

5. **Secure property rights are important for empowering women.**

   
   Access to land rights can help empower women.

   As we saw above, access to assets is essential for women's empowerment. However, millions of women are denied land and property rights for several reasons: many legal systems require women to have a male guardian in order to own property; men may not register their land or property in the name of their wife, and so women lose the property in the event of divorce or death of their husband; despite the fact that women may have the legal right to inherit land or properties,in practice they may be denied these rights by male relatives. Legal reforms are necessary to reduce the vulnerabilities women face as a result of insecure property rights and land tenure.

6. **Secure property rights help secure indigenous peoples' rights.**

   Despite the fact indigenous people have lived on their land for centuries, many countries do not always legally recognize these rights, and take over, or use the land without the consent of the indigenous people. Recognizing indigenous peoples' land rights is not only a human rights issue, but it also makes economic and environmental sense. Once their land rights are recognized, indigenous peoples will be able to use the resources on their land more sustainably, thus improving their economic and social status as a constructive force in society.

7. **Secure property rights are vital for keeping peace.**

   War and conflicts have forced millions of people to flee, leaving their properties behind. Without their property rights legally protected at home, displaced people will not be able to go back to their homes and livelihoods. Peace cannot be fully achieved if land and property rights are not well addressed, potentially triggering further conflict.

> *"Land is vital to our livelihoods. Whether we use it for building a home, operating a business, growing food, or for mere enjoyment, land sustains us all.*
>
> **Source:** Oxfam, Securing Quality and Dignity of Life

What interventionist strategies can promote economic growth and/or development?

Many development strategies aim to grow the economy in the belief that economic growth will lead to economic development. However, interventionist strategies are used to try to ensure that economic growth is inclusive.

Inclusive strategies aim to ensure that the the assets and capabilities of poor people are improved. They directly target the poor and allow the poor people themselves to be directly involved in the process. Such strategies may be implemented by governments or by NGOs.

To be effective, strategies need to be focused towards areas directly associated with the poor. Therefore, they should be aimed at:

- the sectors of the economy in which the poor work (for example, agriculture and the informal economy)
- the areas in which the poor live (for example town ghettos or underdeveloped rural regions)
- the factors of production which the poor possess (ie unskilled labour)
- the products which the poor consume (for example, food).

Economics in action

ATL Thinking, Communication and Research

Go to the United Nations Development Program (UNDP) website: www.undp.org.

1. Find Goal 16, 'Peace, justice and strong institutions' by clicking on the Goal 16 icon.
2. Make a note of the facts and figures offered.
3. View the Goal 16 targets.
4. Evaluate the success of your own country, or a country of your choice, in achieving the Goal 16 targets

Key concept

INTERVENTION

Key concept

EQUITY

How can redistributive fiscal policies promote economic growth and/or development?

In developed countries, fiscal policy can be an effective tool for redistributing income. Governments earn money from taxes, and redistribute through transfer payments. However, developing countries have far less scope to redistribute income this way, because their ability to raise revenues from taxes (their *'fiscal capacity')* is quite limited. As a result, their ability to provide transfer payments and finance merit goods such as health services, education and infrastructure is also limited.

There are several reasons why governments in developing countries struggle to raise tax revenues. Table 31.2 lists some of the challenges governments face in raising taxes along with possible strategies to overcome these.

Challenge	Strategy
The large size of the informal economy, whose economic activity is not taxed.	Strategies to mobilize informal workers and enterprises into the formal sector.
There is heavy reliance on indirect taxes, because they are considerably easier to set and collect, but indirect taxes tend to generate lower revenues. Furthermore, indirect taxes are regressive, so worsen income inequality.	Impose higher taxes on goods such as alcohol, cigarettes, gambling and luxury goods, which are consumed more by high-income people.
Extensive tax exemptions and loopholes in the tax structure, which mean that high income people may not pay their fair share.	Improve the tax structure to remove loopholes and ensure that the tax exemptions are meaningful
High tax rates on high levels of income may give incentives to people to evade paying taxes.	Lower rates of tax at high incomes to encourage people to pay. The lower rate could be offset if more people pay their share.
There are high levels of non-compliance, where people avoid paying taxes. Possible reasons for this include: • corruption in government so that people do not trust the government to use revenues • a lack of transparency in government so that people are not aware of how their tax revenues are used • a weak sense of national identity.	Measures to overcome non-compliance include: • commitments to reduce corruption so that people believe that the tax revenues will be spent appropriately • provide access to details concerning government budgets, so that governments are accountable to the public about what happens with the taxes they pay • public awareness campaigns to increase compliance by teaching people about the role of taxes and building a sense of national identity and responsibility • empower people to engage in open discussions about the uses of taxes.

▲ **Table 31.2** Challenges and strategies for increasing tax revenues

17 PARTNERSHIPS FOR THE GOALS

Sustainable development goal 17.1:

"Strengthen domestic resource mobilization, including through international support to developing countries, to improve domestic capacity for tax and other revenue collection"[10]

[10] **Source:** SDG 17, https://sustainabledevelopment.un.org/sdg17

Economics in action

ATL Thinking, Communication and Research

In its publication, *Building Tax Culture, Compliance and Citizenship*, the OECD shows how governments can use tax education to "transform their tax cultures."

In the publication, they present information on innovative programmes that governments have implemented including:

- a television soap opera called "Binding Duty" in Nigeria
- computer games about taxes in Uruguay
- a "Time for Taxes" calendar in Lebanon
- National Income Tax Day in Bangladesh
- classes on taxes and accounting for businesses in Bhutan
- tax camps for secondary school children in Malaysia to instil a sense of responsibility for paying taxes.

Investigate one (or more!) of these to gain an appreciation of the objectives of the government and to see what they are doing in their programme.

How can transfer payments impact economic development?

Key concept

EQUITY

Governments in developing countries face the challenge of allocating their very limited revenues to investment in merit goods and public goods, such as education, health and infrastructure, which have a significant effect on future poverty, or spending on transfer payments, which tends to have a greater impact on current poverty. In terms of achieving economic growth and development, the gains to investment in education, health and infrastructure are substantial. The complexities and costs of administering transfer payments are also a challenge.

However, a programme that has demonstrated positive outcomes in many developing countries is conditional cash transfers (CCT). Conditional cash transfer programmes are transfer payments targeting low income people. They aim to reduce poverty by making welfare programs conditional upon the actions of the person receiving the money. The government (or a non-government organization) only transfers the money to poor people in return for fulfilling specific behavioural conditions. These conditions may include, for example, children's school attendance, up-to-date vaccinations, or regular visits to a health care facility by pregnant women. CCTs have direct effects on poverty by, firstly, increasing the immediate income of the poor, but also by having a positive impact upon the socio-economic well being of the recipient (and their families). Thus, CCTs can alleviate poverty and improve the quality of human capital.

CCTs do not themselves create jobs, but they permit children more access to education and health care, which will make them more productive in the future and in turn should lead to higher income, taking them out of poverty. The size of the CCT is not enough in itself to raise a recipient out of poverty. It simply adds to the income that the recipient is currently receiving and provides some compensation for parents who send their children to school as opposed to working or begging.

Exercise 31.2

ATL Thinking and Communication

Read the following article and answer the questions that follow it.

The use of CCTs started in the 1990's in Latin America, where one of the first schemes was the *Progresa* program in 1997 (later called *Oportunidades* and now called *Prospera*). This scheme provided cash transfers to households with the conditions of regular school attendance and health clinic visits. It was designed to encourage improved education, improved health care and improved nutrition for poor families.

Conditional Cash Keeps Girls in School

Keeping girls in school has become a priority for those fighting poverty around the globe, and for good reasons. Research shows that the longer a girl stays in school, the more likely she is to delay marriage and avoid early pregnancy. This means lower maternal and child mortality rates, fewer abortions and improved child health. In addition, a 2011 World Bank study shows that investing in girls' continued education can boost labour force participation, lifetime earnings and **GDP**. However, even though it is clear that investing in girls' education spurs economic growth and lessens poverty and social instability, millions of girls around the world still face cultural and economic barriers that keep them out of school.

One way to counter this phenomenon is to offer poor households conditional cash transfers (CCTs). CCTs give money to poor people in return for fulfilling specific conditions, such as accessing basic health services, vaccinating children or sending daughters to school. These programs offer a two-fold approach that breaks the **poverty cycle** by both providing the poor with additional income and also strengthening human capital with healthcare and education services.

The success of one education-specific CCT program, the Female Secondary School Assistance Program (FFSAP), illustrates that providing girls with a small stipend to stay in school has far-reaching benefits. FFSAP, a joint program founded by the World Bank, Asian Development Bank and Government of Bangladesh, provided female students in grades six through ten with a monthly stipend on three conditions: that the girls maintained a 75 percent attendance rate, scored at least 45 percent on their exams and remained unmarried.

According to a study assessing the FFSAP, CCT money enabled girls to extend their education up to two years, which in turn had significant economic and social impacts. Continued education for girls in Bangladesh led to a 3.6 to 10.6 percent increase in women's labour force participation. Girls enrolled in the program also delayed marriage by 1.4 to 2.3 years, which is particularly meaningful given that Bangladesh has one of the highest child marriage rates in the world; 66 percent of Bangladeshi girls are

a) (i) Define the term *GDP* indicated in bold (paragraph 1). [2 marks]

(ii) Define the term *poverty trap* indicated in bold (paragraph 2). [2 marks]

b) Explain how the CCT may break the poverty trap (paragraph 2). [4 marks]

c) Explain **two** factors that might make it difficult for a developing country to promote such conditional cash transfers. [4 marks]

What is the role of minimum wages in promoting economic development?

As established in Chapter 22, the purpose of minimum wages is to "protect workers against unduly low pay and ensure an equitable share in the fruits of progress to all and a minimum living wage to all who are employed and in need of such protection"[11] Therefore the establishment of a minimum wage can be seen as a valuable tool to reduce poverty and inequality. When minimum wages exist, but do not provide a 'living wage' (a wage that ensures a worker can meet their basic needs), a development strategy would be to increase the minimum wage.

Key concept

EQUITY

Minimum wages exist in more than 90% of the 187 member countries of the International Labour Organization, including the majority of developing countries. And while minimum wages are credited with having a positive impact in terms of reducing poverty, and should form part of any poverty-reduction strategy, it is argued that they have only a moderate impact and can not be considered as a major tool to combat poverty. There are a few reasons for this:

- According to an ILO report issued in April 2018, around 61% of the world's employed population works in the informal sector. In Africa 85.8% of employment is informal. In Asia and the Pacific, the proportion is 68.2%. In the Arab States, 40% of employed are in the informal sector[12]. Workers in the informal sector are not under contract, do not receive social protection, are not guaranteed decent working conditions and are not protected by the rule of the law. They may work in dangerous and vulnerable positions. Because workers in the informal sector do not receive any legal benefits or protection, they do not receive minimum wages, and so any policy to reduce poverty through minimum wages will not be effective at reducing the poverty among informal workers. This is one of the many reasons the International Labour Organization emphasises the urgency of tackling informality and promoting the formalization of employment.

[11] **Source:** The International Labour Organization: How to define a minimum wage, https://www.ilo.org/global/topics/wages/minimum-wages/definition/lang--en/index.htm

[12] **Source:** The International Labour Organization: Women and Men in the Informal Sector: A Statistical Picture, April 2018. https://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/documents/publication/wcms_626831.pdf

> "The incidence of informality is a major challenge for the realization of decent work for all and sustainable and inclusive development."
>
> **Source:** International Labour Organization. https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_627189/lang--en/index.htm

- Even in the formal sector, where workers are entitled to receive a minimum wage, there are always issues with "compliance and enforcement". That is, it may be relatively easy for firms to pay less than the minimum wage and escape any form of punishment. In their support of labour throughout the world, The International Labour Organization promotes methods to improve compliance with minimum wages, and advocates measures such as: information and awareness raising campaigns; better design of minimum wage policies; empowering workers to claim their rights through collective action; effective punishments that act as a disincentive to non-compliance; targeted labour inspections and monitoring practices within global supply chains to ensure that multinational companies ensure that legal regulations for labour are being observed when they operate with local suppliers.[13]

- There is a risk that although minimum wages may improve the incomes of some, they may also disadvantage others. It is possible that a minimum wage (or a higher minimum wage) will cause some employers to lay off workers. If those workers live in low-income households, poverty will increase, particularly if the worker was the only earner in the household. Another possible negative outcome is that if workers are laid off from jobs in the formal sector, they may seek jobs in the informal sector, putting downward pressure on wages there.

8 DECENT WORK AND ECONOMIC GROWTH

Minimum wages must not be discounted as a means of reducing poverty. However, their effectiveness is limited by the sheer size of the informal sector, and the extent of non-compliance that may prevent workers from being paid the legal minimum wage. Sustainable Development Goal 8 recognizes these challenges and has set targets to "encourage the formalization and growth of enterprises" and "protect labour rights" for all workers.

Economics in action — ATL Thinking, Communication and Research

Investigate the effectiveness of minimum wages in a developing country.

[13] **Source:** International Labour Organization, How to Enforce Minimum Wages, https://www.ilo.org/global/topics/wages/minimum-wages/enforcement/lang--en/index.htm

How might the provision of merit goods promote economic growth and/or development?

As you know, merit goods are underprovided in a market. Merit goods such as health services and education provide tremendous private and external benefits; but developing countries face the enormous challenge of providing such merit goods. A brief look at the health and education statistics for developing countries reveals a huge range of outcomes, with some countries experiencing tremendous progress in some areas, while others make little progress at all. Yet, regardless of the level of economic development of a country, the gains from effective investments in these areas are enormous, and the key for economic growth and development.

Access to quality health care and education has the potential to raise the human capital of a country's population. Significant challenges exist in terms of identifying the needs, choosing appropriate services, financing the programmes and ensuring that all people have access to the services. Countries face different priorities and these need to be taken into account. These are the challenges that have been clearly identified in many of the Sustainable Development Goals.

To support the economic development of a population, extensive investments must be made in all types of infrastructure, including clean energy, transport, telecommunications, and clean water and sanitation. Again, the challenges of providing appropriate essential infrastructure have been identified throughout many of the SDGs.

The increased supply of merit goods may be provided through many means, such as domestic government investment, foreign direct investment, microfinance, social enterprise or from international cooperation through foreign aid. It is hoped that the commitment made by all countries to the SDGs will ensure that each country can make progress in meeting the challenges of providing these essential merit goods.

Key concept

EQUITY

The Multidimensional Poverty Index

It would be inappropriate for countries to adopt a one-size-fits-all approach to poverty reduction, as the nature of poverty differs from country to country. Look back at the information in Figure 22.7. This demonstrated that Peru and Tajikistan experience similar levels of multidimensional poverty. However, the data shows that children in Peru experience greater deprivation in terms of accessing education than Tajikistan, as schooling contributes 18% to the MPI index in Peru and only 1% in Tajikistan. In Tajikistan, nutrition contributes 35% to the MPI index, while in Peru, the figure is 18%. This information could help governments and international partners devise country-specific strategies to reduce poverty.

How might foreign aid help to achieve economic growth and/or development?

Key concept

INTERDEPENDENCE

Foreign aid is any assistance that is given to a country that would not have been provided through normal market forces. Aid may be provided to developing countries for a number of reasons including:

- to help people who have experienced some form of natural disaster or war
- to help developing countries to achieve economic development
- to fill the savings gap that exists in developing economies
- to improve the quality of the human resources in a developing country
- to strengthen institutions
- to improve levels of technology
- to fund specific development projects

- to enable a country to increase their capacity to benefit from international trade opportunities (Aid-for-trade)
- to help meet the Sustainable Development Goals.

What is humanitarian aid?

Humanitarian aid is aid given to save lives and alleviate suffering in response to emergencies such as natural disasters (eg earthquakes, monsoons, prolonged drought) or human-made crises (eg international wars, civil wars, refugee crises). It may also be used in response to a medical crisis, such as the Ebola outbreak. While essentially short-term in nature, humanitarian aid may be prolonged if a host government is unable to take over control of the crisis and the human suffering continues.

What is development aid?

Development aid is given by governments, multilateral organisations and non-government organisations in order to alleviate systemic poverty and promote the economic, social, environmental or political development in recipient countries. In contrast to humanitarian aid, which is a short-term response to an emergency, development aid is long term assistance in response to systematic problems.

What is "official development assistance"?

"*Official development assistance*" (ODA) is defined by the OECD Development Assistance Committee (DAC) as 'government aid that promotes and specifically targets the economic development and welfare of developing countries[14]'. ODA is given either by a government, through its official aid agency or through any one of the multilateral international institutions to which the country contributes. These include the United Nations and its many affiliated organisations (eg UN Development Programme, UN Children's Fund, UN Industrial Development Organisation, the World Health Organization, the International Labour Organization), the World Bank, and the International Monetary Fund. When a government gives aid directly to another country, it is known as *bilateral aid*. When a government gives aid money to one of the recognised international agencies, it is known as *multilateral aid.*

SDG 17 emphasises the need for the global partnership in achieving sustainable development and target 17.1 specifically identifies the role of ODA in meeting this goal. It calls for "developed countries to implement fully their official development assistance commitments, including the commitment by many developed countries to achieve the target of 0.7% of GNI"[15], as measured by the OECD Development Assistance Committee (DAC).

The DAC has very specific eligibility requirements to measure whether a particular programme meets the criteria to be considered as ODA.

[14] **Source:** OECD, Official Development Assistance, http://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/official-development-assistance.htm

[15] **Source:** Sustainable Development Goals, SDG 17.

To meet eligibility requirements, the foreign aid must be must be provided by official agencies and it must be *'concessional'*; this means that it must be either a grant or a soft loan. A soft loan is a loan which is either interest-free, or at below market interest rates and is usually to be repaid over a longer period than commercial loans. Furthermore, the aid must have the promotion of the economic development and welfare of developing countries as the main objective.

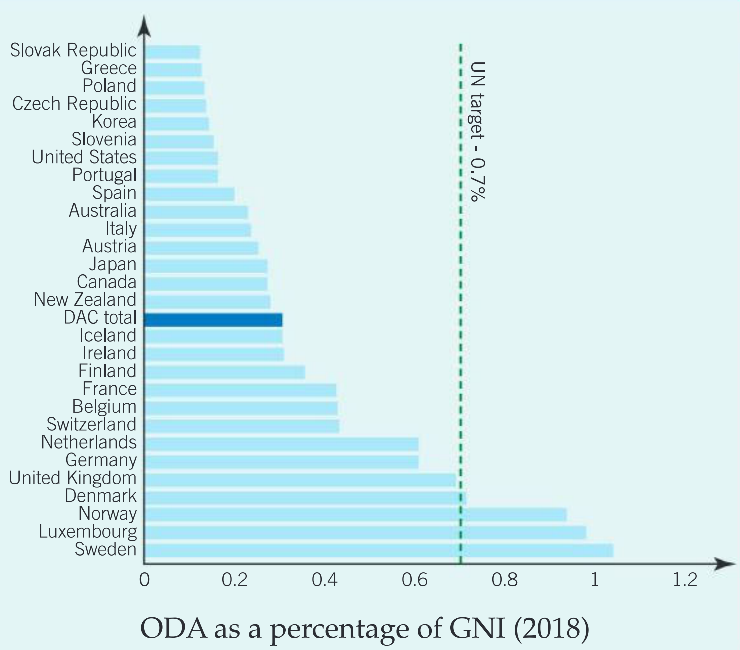
ODA does not include military aid or aid that is donated to pursue the donor's security interests.[16] So, for example, a UK "train and equip" project to strengthen the Lebanese Armed Forces (LAF) Land Border Regiment was deemed 'non-ODA eligible' as it aimed to build defenze capacities of the partner country's armed forces. Similarly, a Portuguese project to support health-care services and medical assistance to treat military personnel of partner countries was also deemed non-eligible as it provides medical care that was not available in the partner country and was aimed at strengthening the military. On the other hand, an Austrian project to strengthen the "Transnational Crime Units" to help police fight against drug trafficking, organized crime and drug abuse in five West African countries was deemed "ODA eligible" as it followed stated rules to help partner country police prevent and address criminal activities.[17] Thus, it could be seen to support domestic institutions of partner countries in a way that benefited the population as a whole.

Economics in action

ATL Thinking, Communication and Research

How are countries doing in terms of meeting the goal of contributing 0.7% of their GNI to ODA?

Which countries are meeting the UN goal? Find the most recent data to see if any improvements have been made.



[16] **Source**: OECD, Official Development Assistance, http://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/official-development-assistance.htm

[17] Examples taken from OECD Financing for Sustainable Development, SDG DAC Eligibility Database, http://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/oda-eligibility-database/

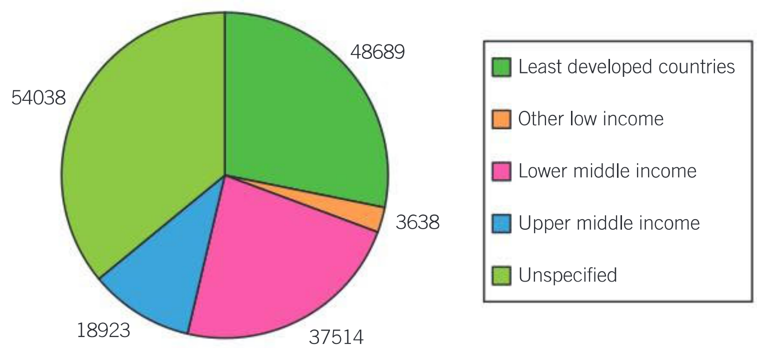
1.1.1. Top 10 ODA receipts by recipient *USD million, net disbursements in 2017*			
1	Syrian Arab Republic	10,361	6%
2	Ethiopia	4,117	3%
3	Afghanistan	3,804	2%
4	Bangladesh	3,740	2%
5	Nigeria	3,359	2%
6	Yemen	3,234	2%
7	Turkey	3,142	2%
8	India	3,094	2%
9	Jordan	2 921	2%
10	Iraq	2,907	2%
	Other recipients	122,123	75%
	Total	162,802	100%

1.1.3. Trends in ODA

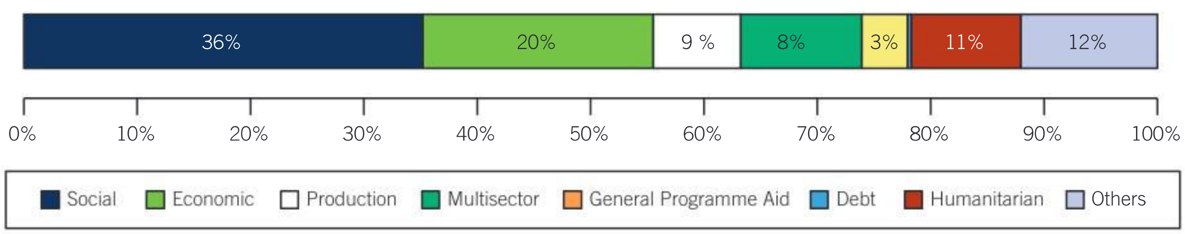
	2016	2017	% change
ODA net disbursements (2016 constant USD million)	158,218	160,780	1.6%
ODA gross disbursements (2016 constant USD million)	181,529	187,511	3.3%
ODA commitments (2016 constant USD million)	186,501	192,946	3.5%
Population (thousands)	6,100,285	6,180,222	1.3%
Net ODA per capita (USD)	25.9	26.3	–

1.1.2. Top 10 ODA donors *USD million, net disbursements in 2017*			
1	United States	30,006	18%
2	Germany	19,818	12%
3	EU Institutions	16,054	10%
4	United Kingdom	11,335	7%
5	IDA	9,513	6%
6	Japan	8,080	5%
7	Turkey	7,950	5%
8	France	6,649	4%
9	Global Fund	4,226	3%
10	United Arab Emirates	3,835	2%
	Other donors	45,334	28%
	Total	162,802	100%

1.14 ODA by income group
USD million, net disbursements



1.1.5. Sectors in 2017
commitments



Source: *World Development Aid at a Glance, 2017*, OECD, www.oecd.org

Figure 31.1 ODA statistics for 2017

Figure 31.1 shows ODA figures for the top developed country donors that are members of the DAC for the year 2017, the main recipients of this aid, trends in ODA, the areas receiving the aid and the uses to which the money was put.

Are there concerns about aid?

To achieve the Sustainable Development Goals, it is clear that international cooperation is required on a vast number of fronts, and it is clear that developed countries have a responsibility to partner with developing countries in order to achieve these goals. Financial support through Official Development Assistance and Non-governmental organizations is one way of doing this.

Nevertheless, there are concerns about the nature, disbursement and uses of aid, which must be addressed as countries cooperate to achieve the global development goals. These concerns include the following:

- If the government in power does not have the welfare of the majority of the population at heart, it may mean that when aid is received, it goes to a small sector of the population or a particular sector of the economy that does not need the support.
- Aid is sometimes given for political reasons rather than being given to countries where the need is greatest. It is argued that the developed countries tend to give aid to those countries that are of political or economic interest to them. One result of this is that the poorest people in the world actually receive less aid than people in middle-income countries.
- Aid is often linked to the political views of the donor governments. If these views change due, for example, to a change in government, then this can have serious consequences for the countries receiving aid.
- One form of bilateral aid is '*tied aid*'. This is when a country gives money for a particular aid project on the condition that the recipient country uses the money to buy goods and services from the donor country. The result may be that the donor country ends up paying more for the goods and services than they would have done in an open market. It also may reduce possible trade between developing countries who may have been able to provide the products less expensively. It calls into question the real motivation for the aid. Some economists have argued that tied aid is often politically motivated and is little more than a subsidy to industries in the donor country. The provision of tied aid has fallen in recent years and it has actually been phased out in some countries.For example, the UK made the giving of tied aid illegal in 2002.
- While the short-term provision of food aid may be essential, long-term provision of large quantities of food may force down domestic prices and make matters worse for domestic farmers.
- Some economists view aid as creating a culture of dependency that can actually limit long term economic development. A country may become so dependent on aid that the the government has little incentive to implement strategies of its own. This will be particularly damaging if the domestic economic situation in donor countries worsen and they reduce the amount of aid that they give.
- Some argue that aid is often focused on the modern industrial sector and may cause a greater gap in incomes and living standards between those in that sector and those in the traditional agricultural sector.
- Aid is often only available if the country agrees to adopt certain economic policies. Donors may argue that aid will only be effective if it is given to countries that adopt what it considers to be "sound" economic policies and these often reflect policies that emphasize the free market principles of liberalization, deregulation and

Key concept
EQUITY

Key concept
CHOICE

Key concept
ECONOMIC WELLBEING

White House moving forward with plan to cancel foreign aid, teeing up fight with Congress

https://edition.cnn.com/2019/08/16/politics/omb-rescission-package-foreign-aid-funding/index.htm privatization to promote economic growth. It is argued that these policies might be more in the interest of the developed countries and its multinational companies and not necessarily in the best interest of developing countries.

- Despite the fact that loans may be concessional, they still need to be repaid. Repayments on financial aid may lead to massive problems of indebtedness for developing countries.

Key concept
EQUITY

Key concept
SUSTAINABILITY

Key concept
ECONOMIC WELLBEING

What are Non-governmental organizations (NGOs)?

Non-governmental organizations (NGOs) have a major role in terms of promoting economic growth and economic development. It is very difficult to generalize about NGOs as they are incredibly diverse—in size, purpose, outlook, nationality, income and success. However, we can say that, for the most part, the priority of NGOs is to promote economic development, humanitarian ideals and sustainable development. Although some NGOs receive funding from governments, they operate independently, without the influence of government. Their work might be to provide emergency relief in cases of disasters or to provide long-term development assistance. Examples of international NGOs are Oxfam, CARE, Mercy Corps, Cafod, Greenpeace, Amnesty International, Global 2000 and Doctors Without Borders (Médecins Sans Frontières).

NGOs carry out two main types of activities. They have operational activities, where they plan and implement specifically targeted projects in developing countries and they carry out advocacy activities where they try to influence public policy in areas such as poverty reduction, workers' rights, human rights and the environment. Some NGOs do one or the other of these activities, and some do both, by actively raising funds and raising awareness of the issues. This can result in public pressure on governments that might affect the amount and type of official aid that is given. They can also influence the buying patterns of consumers in ways that contribute to better working conditions and the promotion of sustainable development.

As NGOs often work directly in the field, it may be argued that they can develop a much deeper understanding of the issues and challenges facing the poor than official aid donors may do. In this way, they can attack poverty directly. They may work in areas that official aid cannot reach and work with groups that might be isolated from official aid. Much of what is done by NGOs focuses on working directly with poor people to enhance their human capital. This may be done in a variety of ways such as literacy programmes, health education, AIDS prevention projects, agricultural education and support, micro-credit schemes, immunization and vocational training.

As noted earlier, many NGOs focus their attention on women in particular, and we have already recognized the value of raising women's incomes and status in achieving overall economic development.

NGOs can be credited with making significant contributions in terms of raising awareness and implementing highly successful programmes in developing countries. And just like any other organisation, NGOs working in developing countries should demonstrate good governance, accountability and transparency in their activities. Nonetheless, there are concerns and criticisms of their work. These include:

- Obviously, NGOs rely on funding in order to carry out their programmes and advocacy work. Such funding comes from a variety of sources including private individuals, corporations, charitable foundations and governments. It may be that what the NGO can or can't do depends on where their funding came from and it may limit the effectiveness of what they do. In theory, NGOs operate independently of a government, but if a significant amount of their funding comes from the government, then their activities will inevitably be impacted by political views. For example, in 2018, the US government enacted a ban preventing any aid organisations receiving US government money for providing abortions or even providing any information about family planning that included information on abortions. This change in funding was expected to have grave consequences on women's health throughout the developing world, with an anticipated rise in maternal deaths due to unsafe illegal abortions.
- It may be the case that there are many NGOs operating in a developing country, resulting in uncoordinated and wasteful activities. For example, an NGO might use health workers in one area, or sector, reducing the availability in other areas. It may even be the case that NGOs draw workers away from local government projects, and thereby undermine the local government's ability to determine how to address an issue.
- NGOs may have a political or religious bias, that determine its activities, and they may promote their own bias on people in other communities.
- NGOs, unlike governments, are unaccountable; they are not elected by the people that they are representing.
- NGOs are sometimes accused of spending more money on advertising and promoting their activities, rather than allocating the money to the actual projects they are operating.

Economics in action

ATL Thinking, Communication and Research

Choose one NGO that works in the field of economic development in a developing country. Put together a report on this NGO, identifying its goals, its strategies, its successes and its challenges. Try to make references to the SDGs. Share this information with your classmates.

As a CAS initiative, you might want to try to do some work with this NGO or raise funds to support it.

How can multilateral assistance contribute to economic growth and/or economic development?

The most well-known providers of multilateral assistance are the World Bank and the International Monetary Fund (IMF).

The World Bank

The World Bank is made up of two closely-linked organisations – the International Bank for Reconstruction and Development (IBRD) and the International Development Agency. The World Bank provides financial support and technical assistance to developing countries, with the purpose of reducing poverty and supporting development. According to its mission statement, "The World Bank has two goals, to end poverty and promote shared prosperity in a sustainable way."[18]

First established following the end of World War II, the IBRD, was founded to lend money to countries in West Europe that needed help re-building their war-torn countries. Nowadays, the IBRD makes loans to middle-income and credit worthy developing countries. The funds for these loans are generated by the issue of World Bank bonds in global capital markets. Repayment of the bonds is guaranteed by the member states and by the government of the borrowing country. Because of this the bonds are seen as very safe and the IBRD is able to get the funds at relatively low interest rates. Thus the IBRD can lend to developing countries at rates that are below the rates that the countries would have to pay if they borrowed the money from other sources.

Economics in action

ATL Thinking, Communication and Research

Pick (at least) one of the World Bank development topics. Research its goals and some of its projects in this area. How do projects undertaken by the Bank help to reach any of the SDGs?

The International Development Agency (IDA) was founded in 1960, and is the part of the World Bank that works with the world's poorest countries. According to its mission statement, "The IDA provides grants and zero-to low-interest loans to the poorest countries to help boost their economic growth, reduce inequalities and improve people's living conditions.[19] The poorer the country, the more favourable the loan conditions.

In its early years, the World Bank tended to provide loans to finance large scale infrastructure projects such as electricity generation and transportation. Nowadays the focus is on smaller scale projects that aim to directly target and benefit the poorest people. A look at their website gives an idea of the huge numbers of programmes in which they are involved and information about all these projects. The projects are grouped into 27 different development topics, shown in Table 31.3. [20]

Agriculture and food	Digital development	Environment	Forests	Health	Poverty	Transport
Climate change	Disaster risk management	Extractive industries	Fragility, conflict and violence	Inequality and shared prosperity	Social development	Urban development
Competitiveness	Education	Financial inclusion	Gender	Jobs and development	Social protection	Water
Debt	Energy	Financial sector	Governance	Nutrition	Trade	

Table 31.3 World Bank Development Topics

The International Monetary Fund

The IMF was proposed at the Bretton Woods Agreements in 1944 at the same time as the International Bank for Reconstruction and Development.

According to its mission statement, "The IMF is an organization of 189

[18] **Source: The World Bank, IBRD, IDA**, https://www.worldbank.org/

[19] **Source, What is IDA?** http://ida.worldbank.org/about/what-is-ida

[20] **Source,** The World Bank Development Topics, http://www.worldbank.org/en/topic

countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth and reduce poverty around the world."[21]

The IMF's primary purpose is to ensure the stability of the international monetary system – the system of exchange rates and international payments that enables countries (and their citizens) to transact with each other. The Fund's mandate was updated in 2012 to include all macroeconomic and financial sector issues that bear on global stability."

The responsibilities of the IMF are set out in its Articles of Agreement as being:

- promoting international monetary cooperation
- facilitating the expansion and balanced growth of international trade
- promoting exchange stability
- assisting in the establishment of a multilateral system of payments
- making its resources available (under adequate safeguards) to members experiencing balance of payments difficulties.

The IMF uses three practices to meet its objectives. These are surveillance, financial assistance and capacity development (technical assistance and training). The IMF conducts an annual in-depth survey of each of its member countries and their economic performance. They then discuss, with the government of the country in question, the policies that are best suited to achieving stable exchange rates and economic growth. This is known as surveillance. These reports are normally published to encourage transparency.

The IMF offers technical assistance and training to its member countries, usually free of charge, in areas such as fiscal and monetary policy, exchange rate policy, banking and finance, and statistics.

When member countries are having problems in financing their balance of payments, the IMF can offer financial assistance in the form of loans. The IMF is funded by a system of "quotas", where each member country deposits money with the IMF. The size of the quota reflects each country's size in economic terms. The loans are made from these quotas. As a condition for receiving the loan, the IMF demands the implementation of a policy programme, agreed by the government of the country and the IMF. Support only continues if the policies are effectively carried out. At the present time, the IMF has approximately $1 trillion available for lending to its member countries.

Working independently, and in partnership with the World Bank, the IMF provides concessional lending through the Poverty Reduction and Growth Trust, at zero interest, and debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative. In 2015, the IMF also created the Catastrophe Containment and Relief Trust. Under the new trust the IMF can join international debt relief efforts for poor countries hit by the most catastrophic of natural disasters and assist those battling public

[21] **Source:** The International Monetary Fund, https://www.imf.org/en/About

Did you know?

The World Bank Group

When we speak about the World Bank, we are referring to the combined work of the International Bank for Reconstruction and Development (IBRD) and the International Development Agency (IDA). In addition to these two organisations, there are three additional organisations that make up the World Bank Group.

These three additional organisations are:

The International Finance Corporation (IFC)

Founded in 1956, the IFC arm of the World Bank group, aims to promote private sector investment in developing countries. The IFC lends funds to private customers to finance development projects in developing countries.The IFC is also involved in giving technical assistance, both to companies and to governments.

The Multilateral Investment Guarantee Agency (MIGA)

Founded in 1988, MIGA promotes foreign direct investment in developing countries to support economic growth and reduce poverty. They do this by selling political risk insurance to MNCs. This insurance covers potential risks such as war, terrorism, the confiscation of assets by the government and the freezing of funds within a country.

The International Centre for Settlement of Investment Disputes (ICSID)

Founded in 1966, ICSID facilitates the settlement of investment disputes between member countries and individual international investors. Over 150 countries are now members of the ICSID.

Key concept

INTERDEPENDENCE

health disasters – such as infectious diseases epidemics – with grants for debt service relief. Three Ebola-afflicted countries (Guinea, Liberia, Sierra Leone) received such assistance, totalling about $100 million in February and March 2015[22].

Both the World Bank and the International Monetary Fund are essential organizations for providing financial support and technical assistance to developing countries. Their overarching goals are consistent with international development goals in general, and the Sustainable Development Goals in particular. Nonetheless, there are concerns about both institutions that include (but are not limited to) the following:

- Both were established in the United States and their neighbouring headquarters are in Washington D.C. Despite their stated goals and the relevance of their projects to economic development and reducing poverty, they have been accused of promoting free market, business-friendly policies which mainly help companies in developed countries and high-income people in developing countries.
- By tradition, the head of the World Bank is appointed by the American president. Clearly, this raises concerns that the chosen person will direct policy in ways that are primarily in the interest of the U.S.
- A particularly negative impression of the IMF is associated with the conditions that it may set on countries who take IMF loans. Following the "Third World Debt Crisis" in the early 1980s, the IMF lent money to countries on the grounds that they would adopt certain policies to reduce fiscal deficits and encourage economic growth in order to be able to repay the loans. These policies were known as IMF Structural Adjustment Policies (SAP). The SAPs, reflected the free market school of thought which dominated the IMF and the World Bank. The policies were known as the Washington Consensus. and commonly included the following free market reforms:
    - ➔ trade liberalization
    - ➔ encouraging the export of primary commodities
    - ➔ devaluing the currency
    - ➔ liberalized capital flows
    - ➔ encouraging FDI
    - ➔ privatization of nationalized industries
    - ➔ elimination of subsidies and price controls
    - ➔ austerity measures to reduce government spending, including spending in areas such as education and health.

IMF Says It Cares About Inequality. But Will It Change Its Ways?

http://thecorner.eu/world-economy/imf-says-it-cares-about-inequality-but-will-it-change-its-ways/81224/

With the focus on economic growth following free market principles, countries may have been able to repay loans, but the consequences of SAPs were widely seen as damaging to the poor, and a failure in terms of contributing to economic development.

With its stated goal of reducing poverty, the approach of the IMF has changed from the days of the SAPs, but concerns remain.

[22] **Source:** IMF, www.imf.org

Exercise 31.3

ATL Thinking and Communication

Read the article and answer the questions that follow:

Ecuador agrees to a $4.2 billion financing deal with the IMF

Ecuador has reached a $4.2 billion financing deal with the International Monetary Fund (IMF), President Lenin Moreno said on Wednesday, as the Andean country grapples with a large **budget deficit** and heavy external debt.

The country will also receive $6 billion in loans from multilateral institutions including the World Bank, the Inter-American Development Bank, and the CAF Andean development bank, Moreno said in a message broadcast on national television and radio.

The OPEC nation's debt grew under former leftist President Rafael Correa. President Moreno earned Correa's support during the 2017 election campaign, but has implemented more market-friendly economic policies since taking office.

President Moreno said the maturities on the loans extended "up to 30 years" and that the interest rates "on average" did not exceed 5 percent. "This money will create work opportunities for those who have not yet found something stable," he said.

Moreno has begun to implement an austerity plan that includes layoffs of workers at state-owned companies and cuts to gasoline subsidies. There are also plans to find a private operator for state-run telecoms company CNT and other state-owned firms. Moreover, allowing for less rigidity in wages and prices could help support external adjustment. This can be achieved through policies that remove rigidities in the labour and product markets and in the financial sector.

Other reforms to make the country an attractive business destination and to boost growth and more formal employment include reviewing the system of taxation and removing obstacles to business formation and operation. Other key reforms include taking steps to encourage private investment, opening international trade and creating better conditions for participation of women in the labour market.

According to the IMF, Ecuador has made substantial gains in reducing poverty and inequality over the past two decades, since the country adopted dollarization (using the US dollar as its currency). Ecuador's gini index fell from 58 in 1999 to 45 in 2016. The percentage of the population living in **relative poverty** has fallen from 64.4 percent in 2000 to 21.5 percent in 2017 and the share of the population living in **absolute poverty** fell from 28.2 percent in 2000 to 3.6 percent in 2016.

While these are notable achievements, poverty rates among the rural and indigenous populations remain high. While social assistance spending is high by regional standards and there is good coverage of those in the bottom 20 percent of the income distribution, the authorities see scope to do more. Therefore, the government included measures in the plan to continue protecting the poor and most vulnerable. These include:

- increasing spending on social assistance programs, such as Bono de Desarrollo Humano, Bono Joaquin Gallegos Lara as well as extending the coverage of pensions
- developing a social registry to improve targeting of social programs
- increasing the efficiency and quality of primary education and health spending to enhance human capital and external competitiveness of the economy.

Skepticism of the IMF runs strong in Ecuador and throughout Latin America, where many blame Fund-imposed austerity policies for economic hardship.

a) Define the following terms used in the article:

i) budget deficit [2 marks]

ii) relative poverty [2 marks]

iii) absolute poverty. [2 marks]

b) Using a Lorenz curve diagram, explain what happened to income distribution in Ecuador from 1999 to 2016. [4 marks]

c) Identify market-oriented approaches that Ecuador has undertaken or is planning to undertake. [4 marks]

d) Identify interventionist approaches that Ecuador has undertaken or is planning to undertake. [4 marks]

e) Evaluate possible consequences of the different types of policies in terms of their effects on economic growth and economic development. [15 marks]

Economics in action

ATL Thinking, Communication and Research

1. Select two countries with HDI index values below 0.500.
2. Go to the website www.oecd.org.
3. Search for "Aid at a Glance, by recipient".
4. Select "Aid at a glance charts – OECD" from the list
5. Select ODA flows for recipients
6. Under "Interactive summary charts by aid (ODA) recipients" choose "Open interactive charts"
7. Select each of the countries you have chosen in the top left-hand corner, recipient country scroll down box.
8. Now write a report, maximum 500 words, where you compare and contrast the amount of aid received, the types of aid received, the sources of the aid and what the aid is used for, for each of the countries.

To help you, the "Aid at a glance" chart for Benin is given below:

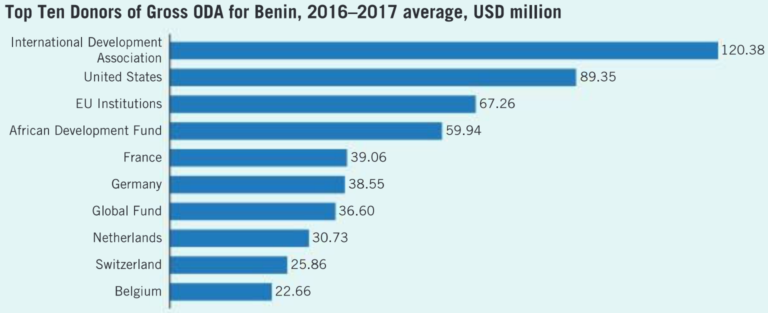
Receipts for Benin

	2015	2016	2017
Net ODA (USD million)	430.1	493.1	675.8
Net ODA/GNI (%)	5.2	5.7	7.3
Gross ODA (USD million)	467.4	529.6	736.9
Bilateral share (gross ODA) (%)	43.3	44.1	45.6
Total net receipts (USD million)	386.3	486.9	748.1

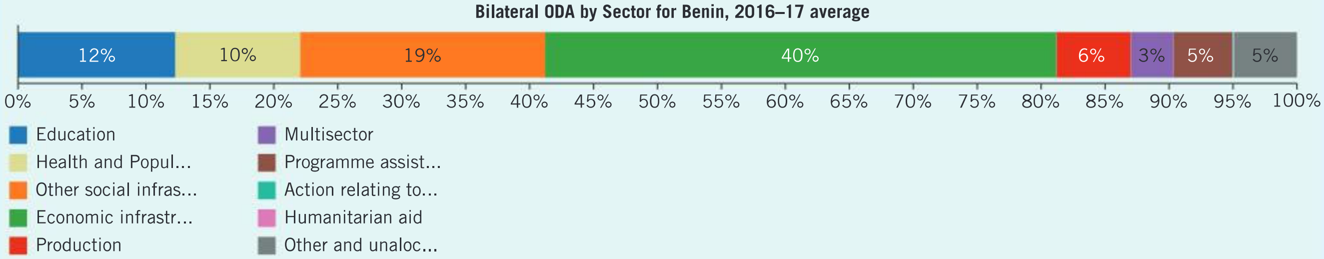
For reference

	2015	2016	2017
Population (million)	10.6	10.9	11.2
GNI per capita (Atlas USD)	870.0	820.0	800.0

Top Ten Donors of Gross ODA for Benin, 2016–2017 average, USD million



Bilateral ODA by Sector for Benin, 2016–17 average



Sources: OECD, www.oecd.org

Total ODA receipts are in the top left table, as is the percentage of bilateral aid. The aid sources are in the top right box. The uses/targets of the aid are given in the bottom boxes.

Economics in action

ATL Thinking, Communication and Research

Research the extent to which investment, loans and aid from China are contributing to economic growth and development in African countries.

Exercise 31.4

ATL Thinking and Communication

Read the article and answer the questions that follow.

Jobless Growth in Bangladesh

According to official statistics, between 2013 and 2016–17, on average, **gross domestic product** (GDP) in Bangladesh grew annually by 6.6 percent, and there has been a net increase of 2.8 million new jobs on top of the 60.7 million jobs that existed in the economy in 2013. This suggests that the number of jobs grew by only 0.9 percent per annum or less than one-eighth of the rate at which the economy grew during those five years. It seems that the growth experienced by Bangladesh is "jobless growth" when an economy experiences growth without a corresponding expansion of jobs.

One of the most alarming features is that manufacturing jobs declined by 0.77 million—from 9.53 million in 2013 to 8.76 million in 2016–17—an annual average decline by 1.6 percent, despite a strong manufacturing output growth of 10.4 percent. While male manufacturing jobs increased by only 0.17 million (from 5.73 million to 5.9 million), female manufacturing jobs actually saw a big drop by 0.92 million (from 3.78 million to 2.86 million). This suggests that the success of generating female employment in the manufacturing sector over the past few decades is at risk now.

One can interpret these outcomes as both good news and bad news. On the positive side, one might argue that labour productivity has gone up due to technological improvement. However, such arguments do not provide any comfort to those who see these numbers as bad news. It is obvious that the economy's rapid growth, which is one of the fastest in the world in recent years, has failed to generate jobs on a large scale, and thus has not been able to translate into the desired reduction in poverty. Consequently, the economy's growth is far from becoming "inclusive growth" as aspired to by the government in its national development plans. This has contributed to widening income inequality too in recent years as is evident from the growing Gini index.

Achieving a high rate of economic growth alone, in terms of a mere increase in the GDP growth rate, should not be treated as a solution for all problems.. The quality of growth is important, and in particular, growth must be able to produce jobs and livelihoods for as many people as possible. In order to avoid "jobless growth", the pattern, structure and strategies of growth have to be revisited. The economic growth momentum needs to be tuned for "meaningful" diversification and structural transformation of the economy where promotion of labour-intensive and high-productivity sectors, both in the farm and non-farm sectors, would be fundamental. This should be coupled with interventions to enhance productivity, jobs and incomes in traditional and informal activities where there are large pools of surplus labour.

Source: Adapted from "An Anatomy of Jobless Growth in Bangladesh', The Daily Star, May 28, 2019 https://www.thedailystar.net/opinion/economics/anatomy-jobless-growth-bangladesh-1572829

a) Use the information from the text to explain why economic growth may not result in economic development. As always, you should try to think of a diagram that you could include.

b) Explain how the strategies suggested by the author might be used to make economic growth more inclusive in Bangladesh.

How can debt relief contribute to economic growth and development?

The IMF published the following regarding the importance of debt relief in pursuing economic development:

- *Debt relief frees up resources for social spending:* Debt relief is one part of a much larger effort, which also includes aid flows, to address the development needs of low-income countries and make sure that debt sustainability is maintained over time. For debt reduction to have a tangible impact on poverty, the additional money needs to be spent on programs that benefit the poor.
- *Boosting social spending:* Before the Highly Indebted Poor Countries (HIPC) Initiative, eligible countries were, on average, spending slightly more on debt service than on health and education combined. Now, they have increased markedly their expenditures on health, education and other social services. On average, such spending is about five times the amount of debt-service payments.
- *Reducing debt service:* For the 36 countries receiving debt relief, debt service paid has declined by about 1.5 percentage points of GDP between 2001 and 2015.
- *Improving public debt management:* Debt relief has markedly improved the debt position of post–completion point countries, bringing their debt indicators down below those of other HIPCs or non-HIPCs. However, many remain vulnerable to shocks, particularly those affecting exports, as seen during the global economic crisis. To reduce their debt vulnerabilities decisively, countries need to pursue cautious borrowing policies and strengthen their public debt management.[23]

Is a new debt crisis mounting in Africa?

https://www.worldfinance.com/special-reports/is-a-new-debt-crisis-mounting-in-africa

Despite improvements, the problem of high levels of indebtedness seems to be rising again. The Jubilee Debt Campaign reported that its study of 126 developing countries revealed that on average, countries were spending more than 10% of their revenues to pay the interest on the money that had been borrowed. This was the highest level of indebtedness since before the 2005 agreement of G7 countries to cancel the debts of the world's poorest countries. There are calls for there to be more accountability in terms of the way that private lenders provide loans to developing countries to avoid the accumulation of debt.

[23] Debt Relief Under the Heavily Indebted Poor Countries (HIPC) Initiative, March 19 2019, IMF

Government Intervention versus market-oriented approaches to achieving economic growth and/or development

Throughout this Course Companion, you have learned about different strategies to achieve economic goals. As you will have seen, they may be grouped into two main categories: interventionist strategies and market-oriented strategies. All of these strategies are employed to achieve economic growth and development, but in many cases, economic growth can come at the cost of economic development and at the cost of sustainability. Therefore, it must be concluded that for any country in the world, regardless of its national income, a complementary package of policies should be adopted when approaching any economic issue, in order to achieve inclusive, sustainable economic development.

Exercise 31.5

ATL Thinking and Communication

The list below is a very simplified summary of the broad types of policies that fall into the categories of interventionist and market-oriented strategies. You should be sure that you can explain what each of them is, provide examples of where they are used and explain the strengths and weaknesses of each of them in achieving inclusive, sustainable economic growth and development.

Market-oriented approaches	Interventionist approaches
• Policies to support competition • Taxes and tradable permits • Deregulation • Privatization • Labour market policies • Tax cuts • Trade liberalization	• Direct provision of merit goods • Direct provision of public goods • Regulations and legislation (command and control) • Consumer nudges • Subsidies • Tax and transfer policies • Price controls such as minimum wages and rent controls • Policies to reduce inequalities • Interventionist supply-side policies • Demand-side policies (to impact short term macroeconomic outcomes) • Trade protection

EXAMINATION QUESTIONS

Paper 1, part (a) questions – HL & SL

1. Explain **two** strategies that might be used to promote economic growth. [10 marks]
2. Explain how increased foreign direct investment might promote economic growth. [10 marks]
3. Explain the difference between import substitution and export promotion. [10 marks]
4. Explain **two** market based supply-side policies that might promote economic growth. [10 marks]
5. Explain **two** areas of institutional change that may promote economic development. [10 marks]
6. Explain the role of the World Bank in promoting economic development. [10 marks]
7. Explain how non-government organizations operate as a means of promoting economic development. [10 marks]

Paper 1, part (b) questions – HL & SL

1. Using real-world examples, discuss the effectiveness of foreign direct investment in achieving economic growth and economic development. [15 marks]
2. Using real-world examples, evaluate the effectiveness of supply-side policies in promoting economic growth and economic development. [15 marks]
3. Using real-world examples, evaluate the effectiveness of foreign aid in promoting economic growth and economic development. [15 marks]
4. Using real-world examples, evaluate the strengths and limitations of strategies for promoting economic growth and economic development. [15 marks]
5. Using real-world examples, evaluate the success of a country of your choice in achieving any **two** Sustainable Development Goals. [15 marks]