CAIE Geography Pre-U

2A: Trade, Debt and Aid

Essential Notes

Global capital transfers

Trade
Trade is the **exchange of goods, money and services between countries and regions**. If a country's imports are greater than their exports then they are said to have a **trade deficit**. If a country's exports are greater than their imports then they are said to have a **trade surplus**.

Foreign direct investment
FDI is the **purchase of land, equipment or buildings or the construction of new equipment or buildings in a foreign country**.

Aid
Aid is the **international transfer of money, goods, or services from a country or international organization** for the benefit of the recipient country or members of its population.

Remittances
Money sent out of a country to someone's home country.

Debt
Money owed to a company, country or person. This can be as a result of **aid or trade deficits**.

Patterns of world trade and its consequences and management

Patterns of world trade

	Importers	**Exporters**
Raw materials	HICs and NICs Cheap to buy	LICs Doesn't make much money
Commodities	HICs and NICs Cheap to buy	LICs Doesn't make much money
Manufactured goods	All More expensive	HICs and NICs High value-added
Services	All but mainly HICs and NICs	HICs Very high value-added
High-tech goods	HICs and NICs Expensive	HICs and NICs High

These patterns of world trade create trade imbalances. HICs and NICs gain a trade surplus whereas LICs have a trade deficit. This means that HICs and NICs can continue growing in wealth by buying cheap raw materials from LICs and adding large amounts of value to it.

Changing patterns of world trade

- **Colonial and neo-colonial patterns:** Colonisers often forced the colonised country to produce fewer types of crops and mainly **produce cash crops** that would produce a lot of money. This meant that when the country became independent, the country's economy was reliant on one crop with not enough food crops. When a country was under colonial influences, most of the resources produced in the country were removed, making it difficult for the country to develop. Neo-colonialism can create **dependency**, exploitation and loss of resources.
- **The rise of NICs:** More goods are being manufactured in NICs due to cheaper labour and greater access to resources. This means that HICs are now focusing on services and design rather than manufacturing.
- **Terms of trade:** A measure of a country's export prices in relation to its import prices. If a country's terms of trade improve, it means that for every unit of export product or service sold it can buy more units of imported products or services. Since the 1990s, LICs have tended to see their terms of trade decrease as a result of increased supply and decreased demand for their primary goods. HICs have seen an increase in their terms of trade as primary products are becoming cheaper with a steady rise in the price of their manufactured goods.
- **The changing nature of goods being traded:** HICs are moving away from manufacturing and specialising in services where they can gain the most value-added. The manufactured goods are now being produced in NICs where there is cheaper labour, but the decision making and investments for these goods are still taking place in HICs. LICs are focusing on manufacturing and exporting one specialised good but are still focusing mainly on exporting primary produce.

Factors contributing to the patterns of world trade

- **Comparative advantage:** Where a country can produce a good or service at a lower **opportunity cost** than another. This creates increasing **interdependence**. It increases the output of all goods and countries can use fewer resources and increase the production of fewer goods. However, transporting goods leads to **pollution** and the use of resources for packaging. It also can lead to **diminishing returns**. By LICs producing goods that they have a comparative advantage in, which is normally primary produce, it means that they are focusing on products which are of lower worth and can vary massively in demand and so in price.
- **Levels of economic development:** HICs tend to trade with other HICs. This makes it harder for LICs to trade.
- **Trade blocs:** Trade between countries increases when they are part of a trade bloc and it makes goods cheaper. However, it means that trading between non-members more difficult and as most LICs are not part of trade blocs it makes it difficult and more expensive for LICs to trade. It also **protects inefficient traders** within the trade bloc and diverts trade away from the more efficient traders outside the bloc. This is known as **protectionism** and it is mainly as a result of tariffs.
- **The World Trade Organisation (WTO)** is an intergovernmental organisation which is concerned with the regulation of international trade between nations. It settles trade disputes, acts as a forum for negotiations, operates a system of global trade rules and supports the needs of developing countries. However, it has sometimes favoured and

supported trade rules which are unfavourable towards LICs, promotes protectionism and has forced LICs to choose **transnational corporations (TNCs)** rather than local businesses and contractors.

Benefits and problems of trade

- **Balance of payments and trade deficits/surpluses:** The balance of payments includes the balance of trade (exports vs imports) together with any invisible earnings and costs such as those from tourism, banking and insurance. Trading can benefit a country if they have a trade surplus as they can then spend this money on improving infrastructure or public services. However, if the country has a trade deficit then money to pay back loans and debt services has to be removed from the money supplying public services such as health and education as well as improving infrastructure.
- **Foreign currency:** Countries may hold foreign currencies in their central bank, these are known as **foreign exchange reserves**. They are mainly kept to ensure that if a country's currency quickly devalues it has backup funds.
- **Overdependence of primary produce:** Many LICs are dependent on their primary products due to the principles of comparative advantage. The prices of primary products are **highly volatile due to inelastic demand** and their production and supply are also volatile as they are **heavily influenced by the weather or natural hazards**.
- **Neo-colonial control:** HICs or TNCs are reliant on LICs for their cheap raw materials and LICs are reliant on HICs or TNCs for trade and infrastructure. This creates dependence but LICs are more dependent on the HIC or TNC and this can put them in a vulnerable position if the country or company decides to move elsewhere.
- **Trade as a political weapon:** Trade and trade restrictions are often used to force policies in countries.

Management of global trade

- **The WTO:** see earlier notes on the WTO.
- **Fairtrade:** is an institutional arrangement designed to **help producers in developing countries gain better trading conditions**. It introduces improved wages for workers, removes discrimination, eliminates the need for child labour due to fair wages, allows small business owners to become competitive on the international market, uses organic techniques and produces are ensured a minimum price no matter what happens. However, there are high fees to join and so small companies might not be able to join, there is a limited base of customers around the world due to higher prices and there is little drive for producers to improve efficiency as they are guaranteed a minimum price.

Patterns of FDI and its consequences and management

Global patterns of FDI

China, Hong Kong and the US were the top three recipients and the top three donors in 2014. Latin American countries had their inward flowing investments increase eightfold between 1980 and 1999. The inflows and outflows for OECD (Organisation for Economic Cooperation and Development eg UK, US, Australia) countries both increased from 1981 to 1999.

Benefits of FDI

- **Improves infrastructure**
- **Invests in the economies of developing countries**
- **Encourages political stability**
- **Offers a large range of consumer goods at cheaper prices**.
- **Offers employment**
- Donor countries are **closer to raw materials** which makes it **cheaper** for them as they have **reduced transport costs** and they can **avoid tariff barriers**.

Role of TNCs

A **transnational corporation (TNC)** is a corporation that is registered and operates in more than one country at a time. They are mainly operating in developing countries to exploit low costs and access to raw materials. They can have massive **negative impacts on the environment** and can **exploit the local population**.

The World Bank

Provides **low-interest loans, zero to low-interest credits and grants to developing countries**. These funds support investments in areas such as **education, health and infrastructure**.

International monetary fund

- Fosters global monetary cooperation
- Secures financial stability
- Facilitates international trade
- Promotes high employment
- Promotes sustainable economic growth
- Reduces poverty around the world
- 0% interest rate on loans to low-income countries

Negatives of FDI

- Exploits cheap labour.
- Profits can leave the country and so won't go to the development of the nation.
- **Caravan capitalism.**
- **Avoid paying full taxes** or receive **subsidies**.
- Lead to environmental degradation.
- Poor health and safety.

Debt

Debt is mainly caused by:

- Overabundant supply of cheap money.
- Insufficient monitoring of aid.
- Loans spent unsustainably.
- Recipient country not generating enough funds to repay the loans.
- Rising world interest rates.
- Countries investing in infrastructure and other economic enticements in order to attract TNCs but this could make them go into debt if they are unsuccessful.

Relieving the debt burden placed on countries can come in several ways:

- **Rescheduling**
- **Debt-for-nature swaps**
- **Debt forgiveness or cancellation.**
- **Debt-for-equity swaps**

The World Bank, the IMF and other multilateral, bilateral and commercial creditors began the **HIPC initiative in 1996**. This structured program was designed to ensure that the poorest countries in the world will not be **overwhelmed by unmanageable or unsustainable debt burdens**. Positives of the HIPC initiative include:

- Gives countries a **fresh start** so they can spend more money on improving their economy.
- There is **flexibility** in the amount of debt relief a country receives.

However, there are also some negatives of the HIPC initiative:

- There are many **complex conditions** and so joining can be difficult.
- More to do with ensuring that the debt can be repaid.
- There are certain **conditionalities** which are tied with the HIPC initiative.
- The debt reduction on offer is **often too small** to make a difference and often the process takes too long.

Patterns of international aid and its consequences

Different forms of aid

- **Long term development aid:** Comes in the form of grants, loans, debt cancellation or technical assistance for supporting long term projects with the aim of improving living standards and the country's economy.
- **Short term relief aid:** The aim is to alleviate a short term hazard after famines, natural disasters or wars in order to get the country back to where it was before the event.
- **Bilateral:** From one country to another, usually is top-down aid so supports big projects with the hope that the wealth with trickle down.
- **Multilateral:** Given by an organisation and is usually in the form of bottom-up aid which involves smaller-scale projects at grassroots.
- **Tied aid:** Where the money made from the project must be spent on goods or services from the donor country.

Majors donors and recipients of aid

OECD countries have a required goal of donating 0.7% of their GDP on aid. Here are the top 5 donors of aid in the world based on a percentage of GDP:

- Norway: 1.07%
- Sweden: 1.02%
- Luxemburg: 1.00%
- Denmark: 0.85%
- UK: 0.72%

The top 4 recipients of aid are:

- Pakistan
- Ethiopia
- Nigeria
- Sierra Leone

Notice how Pakistan receives the most aid even though ranked by GDP per capita it is 133 out of 187, this was mainly due to military aid given by the USA.

Reasons aid is given

- To relieve suffering.
- Improve living conditions.
- Donor country might benefit financially as a result of interest being repaid.
- Donor country may receive a better price on produce.
- Makes allies for potential future conflicts.
- Wins support for the government at home and internationally.

Consequences of aid

- **Corruption**
- Can have a damaging effect on the **environment**.
- Creates **dependency**.
- **Distorts local markets**.
- Skewed towards **political allies**.
- Can introduce technologies which are **too expensive** or are difficult to manage.
- Can **displace poor people**.
- Might only **benefit the richer people** thus increasing **inequalities** within the country.
- Can put pressure on the recipient country and **force tied aid**.

Globalisation

Globalisation is the process of increased interconnectedness among countries through an increased variety and volume of cross border transactions.

Causes of globalisation

- **Improved transport**.
- **Containerisation**.
- **Improved technology** allows better **communication** and sharing of resources and information worldwide.
- Reducing national barriers as a result of **trade blocs.**
- Growth and spread of **multinational corporations and transnational corporations.**
- **Increased mobility of labour** which increases the transfer of money in the form of **remittances.**

Positives of globalisation

- The global competition encourages **creativity and innovation** and **keeps prices in check**.

- Developing countries are able to **benefit from current technologies**.
- Governments are able to **work together towards a common goal**.
- Greater access to **foreign cultures**.
- Developed countries becoming **more aware of the issues facing people in the developed world**.
- **Free movement of labour** around the world.

Negatives

- **Outsourcing** takes jobs away from one country.
- **Cultures can become diluted**.
- **Spread of disease**.
- **Invasive species**.
- **Little international regulations**.
- **Makes the rich richer** and allows more **exploitation of poor people.**
- Free movement of labour can lead to a **labour drain**.
- **Overconsumption**.
- **The deindustrialisation** of HICs can leave derelict buildings and cause chemical and industrial waste to leak into water supplies and soils.