Edexcel Economics A-level

Unit 4: The Global Economy

Topic 6: Measures to Promote Growth and Development

6.3 Other strategies

Notes

- **Industrialisation: the Lewis model**

- The Lewis model is an explanation of how a developing country which focuses on agriculture could move towards manufacturing.
- It is based on the assumption that in agriculture, there is a surplus of unproductive labour in developing economies. The model assumes that in the manufacturing sector, wages are fixed. Workers from agriculture are attracted to the higher wages in the manufacturing sector.
- In the manufacturing sector, entrepreneurs charge prices above the wage rate, which allows them to make profits. It is assumed these profits are invested into more fixed capital for the business.
- The demand for labour increases since the productive capacity of firms has increased. Since there is surplus labour in the agricultural sector, this labour is employed in the manufacturing sector.
- This grows the manufacturing sector to the extent that the economy moves from agriculture to manufacturing. This is from a traditional state to an industrialised state.
- However, in reality, profits might not be reinvested into the firm. Moreover, the capital investment might replace labour, so the demand for labour could fall instead. Also, it is not always easy for labour in the agricultural sector to move to the manufacturing sector.

- **Development of tourism**

- Tourism can create thousands of jobs and help shift a developing country away from dependency on primary products. Developing countries tend to have a marginal propensity to consume, which could create a multiplier effect.
- It helps to diversify the economy and it could make the country more attractive to FDI, as well as developing their infrastructure.
- Tourism accounts for 6% of world trade and 9% of global GDP. For LDCs, about 8% of exports are from tourism. It is one of the largest and fastest growing sectors in the world. Since it is an outward-looking policy, it is considered a more modern way to grow an economy, and the benefits are similar to those of free trade.
- Tourism can also be a way of earning foreign currency for developing countries. The low technology and labour intensive work in tourism is suited to LDCs.

- However, little revenue is retained in the country, since travel agents and hotel owners are likely to repatriate their profits. Moreover, there is the issue of overcrowding and the loss of habitats.
- Income from tourism is likely to be unstable, since it relies heavily on the business cycle in developed countries.
- Investing in tourism can be risky and expensive, however. States have to focus where tourism is attracted, such as transport, land availability and improving infrastructure.
- Locals could feel stigmatised by tourism, especially if they cannot afford the luxuries that the tourists have. There could also be some environmental damage, such as pollution.
- Sri Lanka is trying to develop its tourism industry by building more hotels. It is expected that $1 billion of revenue could be made. It requires very good infrastructure, such as roads and electricity.

- **Development of primary industries**

- Some developing countries have an abundance of raw materials, so some governments might choose to exploit this advantage and develop the industry so the country can have a comparative advantage in its production.
- Moreover, primary industries, especially those allied to farming, form the livelihoods of the bulk of the population. It is sometimes the only source of income for most families. Therefore, it is important that the industry is supported.

- **Fairtrade schemes**

- Fairtrade schemes ensure that farmers can receive a fair price for their goods. Supermarkets buy a guaranteed quantity at a price above the market equilibrium. This helps farmers since they have a guaranteed income and certainty about their sales, so they can plan for the future.
- Fairtrade can help support community development and social projects, as well as ensuring working conditions meet a minimum standard.
- It encourages sustainable production, promotes environmental protection, and stops the use of child labour.
- Critics say the impact of Fairtrade schemes is insignificant. They argue that Fairtrade is simply a psychological influence on consumers in developed countries, who believe they are helping by buying Fairtrade goods. Fairtrade could distract from

other policies and development, and it could make producers not part of Fairtrade worse off. This is since it divides the market into Fairtrade and non-Fairtrade markets. It could be argued that by distorting price signals, Fairtrade is less efficient.

- Fairtrade increases the price of goods such as Cocoa and bananas. This encourages farmers to produce more, which increases their supply. The Fairtrade farmers still get their minimum price, but those not on Fairtrade have to deal with a lower market equilibrium price, due to the increase in supply.
- Fairtrade could make farmers reliant on the sale of their produce, but it promotes self-sufficiency and encourages them to be independent. It has its limitations, but it provides a sense of community, working with farmers, rather than for them.

- **Aid**

- Africa has been a top recipient of Chinese aid. By the end of 2009, it received 45.7% of China's cumulative foreign aid. It is important as a policy instrument for China with engagement with Africa.
- Consumers in LEDCs have a higher propensity to consume than save, due to their limited incomes. Capital inflows, including those in the form of aid, can help fill this savings gap.
- Aid provides temporary assistance to a country, such as humanitarian aid offered to countries after conflicts or natural disasters. Aid could also be a grant for a project that a country might not have the funds for.
- Aid could be used to reduce human capital inadequacies or to pay off debt. It can improve infrastructure, which can help make the country more productive.
- However, the benefits of aid are limited by corrupt leaders, the size of the aid payment and the potential for the recipient country to become dependent on aid.
- Dambisa Moyo and Jeffrey Sachs are two prominent economists who have looked at the effects of foreign aid. Dambisa Moyo is generally against aid, whilst Jeffrey Sachs is generally pro-aid. It is worthwhile to have a look at some of their research and ideas. To briefly summarise, two of Moyo's arguments are that corruption means aid does not go where it is intended and that dumping goods, such as mosquito nets, into a country means private firms cannot compete and are forced out of business. Sachs suggests that it is possible for rich countries to meet the UN MDG of investing 0.7% of GDP into developing countries, which can help them improve infrastructure, yet this target is not being met.

- **Debt relief**

- Debt relief is the partial or total forgiveness of debt.
- In developing countries, debt is considered to be a principal cause of poverty, since it causes human suffering and misery, and it hampers development.
- With high levels of debt, financial resources are diverted from infrastructure, education and healthcare. The country's ability to pay the debt, not the size, is most important. If a country defaults on its debt, it can make it hard to borrow more money in the future.
- Debt forgiveness can allow a country to import more and increase the population's standard of living. It improves government finances, so public services could be funded instead.
- However, if debt is forgiven, it could encourage more borrowing in the future. Moreover, there could be corruption.