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Creating a Sustainable Economic Future for Developing Countries

**Introduction:**

Since the onset of globalization, global economic inequalities have become even more polarized. This onset has created a dichotomy of world economies with the majority of the world’s population living in the bottom half economically. Moreover, struggling developing economies have tried a myriad of solutions with little to no avail. Thus, the goal of this paper is to describe, analyze, and finally choose an economic solution that provides adequate framework for developing economies to work within and to help stifle the growing inequities in the global community.

**Description**

There are a prolific amount of economic solutions that have been posited by developing nations to create a strong economic framework. Therefore, to better understand the different positions taken by countries, economic solutions will be broken down into two categories: small scale and large scale economic solutions. Large scale economic solutions are solutions that are top down initiatives that are predominantly taken by the country’s government. Small scale solutions can come from non-governmental organizations (NGOs) or from the government. This paper will focus on two small scale initiatives, microcredit and land reform, and three large scale initiatives, trade liberalization, Bolsa Familia, and the National Economic Empowerment and Development Strategy (NEEDS).

**Small Scale initiatives**

The first initiative that should be focused on is microfinance. This system is best described as an economic system in which “microfinance covers a much broader spectrum including credit, savings, insurance, and financial transfers.” (*Essentials*, p. 316-317). Microcredit was a system created with the thought of “the need to improve access to capital” (*Essentials*, p. 316). This system of loans is normally targeted at startup businesses and individuals who hail from the lowest socio-economic sector. This system of small loans was first coined by The Grameen bank and later followed by the private firm Kiva who respectively have loaned 10 billion dollars and 235 million dollars. This system of small-scale loans has been implemented in varying countries with varying degrees of results, but most importantly, this system is a small scale effort to provide capitol to the most impoverished sectors of economies and then watch the economy grow from the bottom up.

The second small scale initiative that needs to be focused on is the idea of formally establishing property rights in informal economies. The idea of establishing property rights was created because “economic underdevelopment has been in large part a function of weak property rights” (*Essentials* p. 316). Thus, the idea of reestablishing property rights was created by Hernando Desoto who argued, “there is a vast amount of ‘dead capital’ – that is, land, homes, and business whose owners lack basic property rights such as clear title to ownership” (*Essentials* p. 316). This system again starts at the bottom of the economy, hoping that giving basic property rights to the poor gives them access to a new source of capitol. Just like microfinance, this system has been used in various countries, mostly Latin American, with varying degrees of success.

**Large Scale initiatives**

The first large scale initiative that has been implemented in several countries is trade liberalization. This is perhaps the broadest large scale initiative. Trade liberalization works to “favor agricultural and other exports from the poorest countries, tied to the goals of the MDG” (*Essentials,* p. 317). Trade liberalization will often create an export oriented economy that attempts to trade with more developed nations like the United States. This top down system often includes the opening up of local markets and removal of tariffs (*Essentials,* p. 317). The two countries who have implemented this initiative that will be focused on in this paper are India and Mexico, whose experiences with trade liberalization will be further explored later.

The next large scale program is called Bolsa Familia, or Family Fund. This system was established throughout Brazil in 2003 and “pays monthly small cash stipends to Brazil’s poorest families on the condition that recipient’s children attend school and receive medical attention” (*Cases*, p. 612). These efforts were made trying to solve Brazil’s massive inequality as it is “the most unequal country in the world” (*Cases,* p. 611). The most similar program this could be compared to is the United States’ social security system; however, this system has more parameters on what recipients can do. Brazil is the only country in the world to implement this program to date.

The final large scale program is Nigeria’s National Economic Empowerment and Development Strategy, which from here on out will be written as NEEDS. NEEDS is the most comprehensive large scale program and it takes several steps to help eliminate corruption and improve Nigeria’s economic prosperity (*Cases,* p. 719). This system has several steps in implementation as described in *Cases*:

“First, it increased the transparency of government finances, for example, by auditing the accounts of various levels of government to oversee how money was being spent and by making the findings available to the public. Second it prompted the government to address the corruption problem and improve the rule of law, in part by creating an Economic and Financial Crimes Commission to pursue theft and money laundering” (*Cases,* p. 719).

The program’s implementation has been extremely extensive. Nigeria is the only country that has implemented NEEDS, but the system shows an overarching theme in Africa for the need to remove corruption from politics.

**Analysis**

**Microfinance**

Microfinance’s system of giving out small loans has generated a large amount of ground in the international community. As such, it’s important to focus on what would happen if implemented in a developing economy. First, implementing microfinance would generate a considerable amount of capital inside a developing economy as it provides loans and other forms of monetary stimulus. This is incredibly important as “some scholars have emphasized the need to improve access to capital that is normally unavailable to the informal economy except at exorbitant rates” (*Essential.* P. 317). By providing low cost loans to start-up businesses and the impoverished community, microfinance creates a sustainable source of capital that can be paid back to the organization or individual giving the loan, creating a new revenue stream in the economy. Furthermore, microfinance formalizes that economy by adding institutions that even underdeveloped economies normally regulate, such as loans and other financial transactions. This formalization then creates more taxable industries and a steadier flow of money that can be considered in matters of the state.

Outside of formalizing and providing new sources of capital, microfinance also connects the underdeveloped to the developed world, as illustrated through the for profit organization Kiva, which “helps link people in rich and poor countries” (*Essentials,* p. 317). The connection created helps to bridge global inequality and more evenly distribute money across the globe. With over 10 billion 235 million being distributed by Kiva and Grameen bank, microfinance has generated stable revenue streams from the world’s richest to the world’s poorest (*Essentials.* p. 317.) Helping to bring more investment in the developing economy can introduce outside revenue flows that successfully establish a strong economy.

Thus, in a developing economy, the introduction of microfinance offers a bottom up solution which has an internal and external impact on the economy. Internally, it drafts a new revenue stream and more capital for the government to work with. This helps to generate a more stable investment in the government’s bonds and promotes a more stable lower class because they have more access to capital themselves. Externally, microfinance creates a framework for foreign direct investment in the form of loans. This can generate more interest in an economy, and introducing it would do so.

Microfinance also possesses several drawbacks, too. One major drawback is microfinance’s community financing system. This system “is often funded through nonprofit organizations, and in some cases the borrower is also held accountable to other borrowers in a local association, in that a failure of one individual to repay limits further loans” (*Essentials,* p. 317.) As a result of this, one individual deviating from payments can have a domino effect in a community and cause for individuals who rely on microfinance as a source of capital to suddenly be left without revenue streams. Quickly, this can snowball into removing a key revenue stream out of the economy, affecting the poor and the small businesses.

Another drawback to microfinance is its ability to screen borrowers. As pointed out in the *Essentials* book, microcredit programs often “fail to screen borrowers properly, problems that can lead to indebtedness and default” (*Essentials*, p. 317.) This lack of oversight means that loans can be given to individuals who misuse the money and borrow without the intention to pay back the loan. Unfortunately, this can make microfinance organizations vulnerable to a corrupt borrower and thus lose their own revenue, preventing further action inside the developing country.

Implementing microfinance in a developing country would result in a system that is prone to domino defaults and poor oversight. This means a developing country could quickly lose a key revenue stream to this drawback and thus fall back into economic stagnation. Furthermore, this system would give the government little oversight, as most of the money comes from non-profit and for profit organizations. Thus, implementation of microfinance has its own advantages and disadvantages in a developing economy.

**Property Rights**

Property rights is the second small scale initiative a developing economy can use to implement economic reform. The first advantage that can be seen in opening property rights is its ability to open new sources of revenue. The first way this can be done is by “codifying existing informal institutions and ensuring effective state protection” (*Essentials*, p. 316). When this is done in a developing economy, land owners suddenly have more ability to sell their land or lease it out to prospect buyers knowing that their transactions are legitimate by the state. This trust built with the state opens up a new aspect of the economy, as many land barons may be more trusting of leasing land knowing that the state recognizes their land claims.

Along with a formal recognition of land comes another area a developing economy can tax. The development of “formal property rights would allow for the development of credit as well as allow states to tax and regulate the economy” (*Essentials,* p. 316). This new product of taxation can generate a developing economy more revenue and thus allow for more money to build economic growth. Furthermore, this can result with less “loose money,” or money that goes unregulated through the economy. Thus, more revenue is being tracked inside the country and gives more back to the economy instead of simply adding to the revenues of the land owners.

Formalizing property rights does have its own ill effects on a developing economy. One can be that the state itself can soil this process because “corrupt and highly bureaucratic state controls often deter individuals from starting formal business” (*Essentials,* p. 316). In a developing economy, a corrupt state could formalize property rights with the will to extort land owners. Doing so would deter these individuals from actually doing business with the government and instead create a black market where the government can no longer gain any revenue from the land.

Another issue with property rights and the land reform is that it can often only benefit the elite and not distribute the wealth. This is most demonstrated with Latin American countries and is shown in the *Essentials* book when it states:

“One area that has attracted great deal of attention is land ownership and land reform. In many countries, agriculture is a powerful economic and political force. This is especially the case where agriculture takes the form of large landholdings, which concentrate power in relatively few hands so that much of the population works land they do not own” (*Essentials,* p. 318).

By concentrating the power and political force with landowners, countries can do their own economies a disservice by creating an elite branch of its economy that would use corruption and other methods to keep its power. Furthermore, this would only concentrate on the wealth, leaving a large majority of the population behind and fail to create a middle class, a necessary element to any fully developed economy.

**Large Scale**

**Trade Liberalization**

Trade liberalization is one of the most common methods that developing economies use to grow into a developed economy. One major advantage to liberalizing a developing economy is its ability to open up the economy to privatization. For instance, in many developing economies “restrictions on foreign investment have been eased and many state-owned companies have been sold to the private sector” (*Cases,* p. 459). Opening up the economy to privatization allows to ease the burden of creating resources for exportation and internal distribution and instead drafts more sources for taxable revenue. Moreover, this can help to increase foreign investment in an economy and thus garner the economy multiple revenue streams instead of just the state’s own coffers.

Another promising effect trade liberalization can have on a developing economy is its ability to decentralize an economy’s needs, as shown through the Brazilian case study who after implementing trade liberalization had industry account for one-quarter of GDP and agriculture accounts for 4% (*Essentials,* p. 559). The result of the Brazilian situation can be applied to other developing economies who often rely on one area, whether it be oil, agriculture, or cheap exports. Trade liberalization would open up the economy to diverse sectors and create a more equal revenue stream that’s not reliant on any single sector’s value.

One distinct disadvantage of trade liberalization is its ability to create a new sector that grows unevenly. While it was aforementioned that trade liberalization in Brazil resulted in new sectors in India, it resulted in an overreliance on the IT sector, as shown in the *Cases* book “India faces an additional problem. Although the economy is growing it is doing so unevenly.” (*Cases,* p. 460). The uneven growth in a sector can correlate into a country having an unequal economy, as India does with those in IT vs. those in agriculture. This uneven distribution can generate wealth inequalities, and more importantly, stop any gains liberalization creates by re-establishing an elite class and an impoverished class while devastating any chance of a middle class.

Another issue found in trade liberalization is the flood of cheap goods that often follows the freeing up of importation. This situation is best described in the Mexico case study when it states, “opening up Mexico to a flood of cheap agricultural imports, the government in effect devastated many of Mexico’s poorest peasants” (*Cases,* p. 559). By opening up its borders to cheap goods, especially agricultural goods, a developing economy could destroy its poorest workers in the agricultural industry. This would result in the poor getting poorer, and in the short term, at least, harm the country’s growth. Thus, trade liberalization could quickly change the country into an importer and cause a net loss in its import export ration.

**Bolsa Familia**

One top down initiative that’s case specific is the Bolsa Familia program in Brazil. One major triumph of this program was its ability to target poverty and eradicate its effects. For instance, “By the end of 2010 the program had reached over 11million families (a quarter of Brazil’s population) and is currently the largest targeted welfare program in the world” (*Cases,* p. 612). Moreover, because the program mandates education and health screenings (*Cases,* p. 612) it helps to educate the most impoverished, giving them skills necessary to rise out of poverty and to stay healthy. Implementing a program like Bolsa Familia in a developing economy would establish a program specifically geared at establishing a long term sustainable option for the economy. More importantly, by handing out the money, it gives the impoverished enough money to help alleviate many symptoms of poverty and thus let families focus on becoming more successful and not merely focus on the issues currently at hand. This paradigm creates long-term sustainability in an economy where education is key.

Yet, Bolsa Familia has statistically failed at adequately spending its money on education. For instance:

“The Cardoso, da Silva, and Rousseff administrations increased spending on Brazil’s education system and produced a marked improvement, but a disproportionate amount of state spending continues to be directed towards a higher education system that benefits the economically advantaged” (*Cases,* p. 611).

The differences in education can render a large portion of Bolsa Familia’s efforts as a failure because it funnels the impoverished into an education system that still favors their wealthier counterparts. Thus, implementing this program in a developing country could face similar impediments with an unequal education system that would still stifle the poor and render the education guidance as ineffective.

**NEEDS**

The Nigerian NEEDs program is another top down program that has had relative success for Nigeria’s distraught and developing economy. The most successful part of this system is its long term ability to assess economic needs inside of Nigeria and implement policies to address them. Nigeria’s projects have included several measures. Some of “These measures have included restructuring Nigeria’s foreign debt, modernizing its heavily indebted banking system, and beginning to address the country’s dismally inadequate economic infrastructure in areas such as power generation and transportation” (*Cases,* p. 720). By restructuring its debt, Nigeria has given itself the ability to effectively sell its bonds abroad. Fixing its economic infrastructure creates an internal source of jobs through construction and long term economic sustainability with proper infrastructure. A developing economy implementing these facets would be able to give itself more jobs and help to make it look like a more stable investment to the International Monetary Fund, developed economies, and private corporations. This would ensure long term growth.

Implementing the NEEDS process, however, is no small undertaking. In Nigeria, most of the money is predicated on “the critical factor of oil” (*Cases,* p. 721). As such, the Nigerian government has needed a large amount of money and a steady flow of it to implement NEEDS. Thus, a developing country would need several sources of revenue or a large source of revenue to fully implement the NEEDS program and, in a developing economy, this could turn into an all-or-nothing gamble with its funding sources. This could result in an unsure economic future for an already precarious economic situation.

**Evaluation**

To fully understand which economic initiative is best suited for a developing economy, two criteria must be met for it to be a viable and successful initiative. First, the program must have proper oversight to hedge against the often corrupt practices that are rampant in most developing economies. Second, the program must implement controls that benefit the short term and long term sectors of the economy. In this rational, both bottom up initiatives are immediately disqualified because they do not meet proper oversight, as microcredit often doesn’t check the backgrounds of its borrowers and can leave the country whenever it sees fit, taking with it the capitol it brought. Land reform is another failed bottom up initiative because, while it does allow for the government to regulate land, it still leaves a major amount of autonomy to the land owners who can subvert regulations and flaunt the government’s will, especially if the government is too weak to enforce its rule of law.

Thus, the three top down initiatives are left. Trade liberalization is the next initiative that falters under the second criteria. The reason for this is that, short term, it can ill affect the economy by allowing for a rush of cheap imports. This can devastate the lowest socio-economic bracket and hinder further growth. As such, it is disqualified because it does not meet short term economic prosperity. The NEEDS program again fails with similar logic. As pointed out earlier, the program requires a massive upstart cost for its ambitious goals. Thus, in the short term, massive spending could quickly accrue debt and an all or nothing gamble. This gamble then translates into long term instability violating both facets of the second criteria.

Therefore, Bolsa Familia is the best choice for a developing economy because it implements a policy that can be regulated by the government and because it establishes short term and long term economic stability. The short term is taken care of by the stipends paid to the impoverished families. The long term is taken care of by educating its poorest citizens and translating that into a more educated poor class that eventually can become the middle class with a degree from a higher education institute. Thus, a developing country implementing this program would see its lowest socioeconomic bracket have more capitol to spend through the stipends and in the future, see its impoverished class gain an education and receive higher paying jobs.

The only problem this paper posits with Bolsa Familia is that Brazil has a massive problem with unequal education systems. In another developing country, this could quickly become a problem as well; however, establishing an educated lower class can make this a self-eradicating problem. The reason for this is that the impoverished can have access to capital and an education to achieve the skills required to enter the workforce. After one generation, this can result in an individual raising themself from the lowest bracket to the middle class by having a job that would generate a stable income. Following this, the next generation would be raised in a middle income household and thus be more likely to have the tools necessary to eradicate the inequities in the education system.

As with any economic solution, the Bolsa Familia solution would take time to have the best results. Yet, in a world with rising inequalities, there is no quick fix. Instead, countries must develop long term solutions that can satisfy short term economic solutions. This is best done by the top down initiative Bolsa Familia. After addressing several bottom up initiatives and top down initiatives, it can be evident that no solution is without its issues; however this paper finds that Bolsa Familia with a top down approach would result in the best economic future for a developing economy.

Works Cited

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