



CHAPTER

17

Developing Countries

Why It Matters

Your pen pal from abroad has asked for your school's help on a project to improve the quality of life for the students in his school and community. As a member of the planning committee, your task is to suggest ideas. Create a list of ways to help students and the neighborhood as a whole. Present your proposals to the class. Read Chapter 17 to learn about the ways that developing nations can improve the quality of life for their citizens.

The BIG Ideas

1. Every society has an economic system to allocate goods and services.
2. The study of economics helps us deal with global economic issues and global demand on resources.

► Foreign investments help developing countries by bringing jobs and technology, such as in this optical chip factory in Mexico.



Economics ONLINE Chapter Overview Visit the *Economics: Principles and Practices* Web site at glencoe.com and click on *Chapter 17—Chapter Overviews* to preview chapter information.



SECTION

1

Economic Development

GUIDE TO READING

Section Preview

In this section, you will learn that developing countries face a number of obstacles that make economic growth difficult.

Content Vocabulary

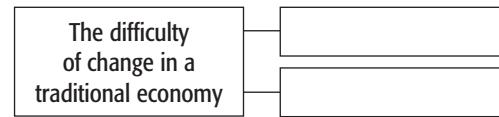
- developing country (p. 469)
- primitive equilibrium (ZPG) (p. 472)
- takeoff (p. 473)
- crude birthrate (p. 474)
- life expectancy (p. 474)
- zero population growth (ZPG) (p. 474)
- external debt (p. 475)
- default (p. 476)
- capital flight (p. 477)

Academic Vocabulary

- proportion (p. 472)
- primary (p. 475)

Reading Strategy

Identifying As you read the section, complete a graphic organizer similar to the one below by identifying at least two reasons why it would probably be more difficult to bring about change in a traditional economic system than in a market economy.



PEOPLE IN THE NEWS

—www.cbsnews.com

Bono's War On Poverty

Actor Brad Pitt is among the celebrities featured in new public service announcements for a war on poverty and AIDS led by U2 singer Bono.

The Irish rock star and political activist says that instead of being focused on donations, the ads for "ONE: The Campaign to Make Poverty History" are aimed at increasing public awareness of the problem and recruiting new advocates for the goals of the campaign.

Pitt, who visited Africa after being inspired by Bono's advocacy, said he was struck by how extreme poverty there has made it difficult for the sick to gain access to drugs to minimize the effects of AIDS. "I've seen it, I've been there, and to walk away from it and turn my back makes me culpable," Pitt said. "I can't do that." ■



Most of the people in the world today live in **developing countries**—countries whose average per capita GNP is a fraction of that in more industrialized countries. Poverty is rampant in most of these countries, with about 1 billion people worldwide now living on the equivalent of less than \$1 per day.

There are many ways to deal with poverty, including direct government aid and voluntary civic organizations. As we read in the news story above, assistance sometimes comes from unexpected sources. Even so, the best way to improve the lot of impoverished people in all nations is with economic growth and development.

developing country country with relatively low average per capita income and less developed infrastructure, education, and health care system



Skills Handbook

See page R43 to learn about **Comparing and Contrasting**.

The Importance of Economic Development

MAIN Idea In a global economy, the economic health of all nations is important.

Economics & You Do you remember reading about poverty in the United States? Read on to learn how this compares to poverty in the rest of the world.

Poverty, whether domestic or global, is more than an economic problem—it is also the source of social discontent and political unrest. It can even threaten the very stability of a country.

In order to make comparisons between countries, economists convert all currencies to a common unit such as the U.S. dollar. Then, to compensate for populations of different sizes, they express all income on a per capita basis.

International Comparisons

The map in **Figure 17.1** shows the total national income for most countries in the world. The United States, which has the largest total income, is the largest area on the map. Countries with smaller incomes are scaled accordingly.

The map is also color coded to show countries with similar national incomes on a per capita basis. Viewed this way, the map clearly shows the contrast between the industrialized economies of North America, Western Europe, and Japan and the developing countries of South America, the Caribbean, Africa, and Asia.

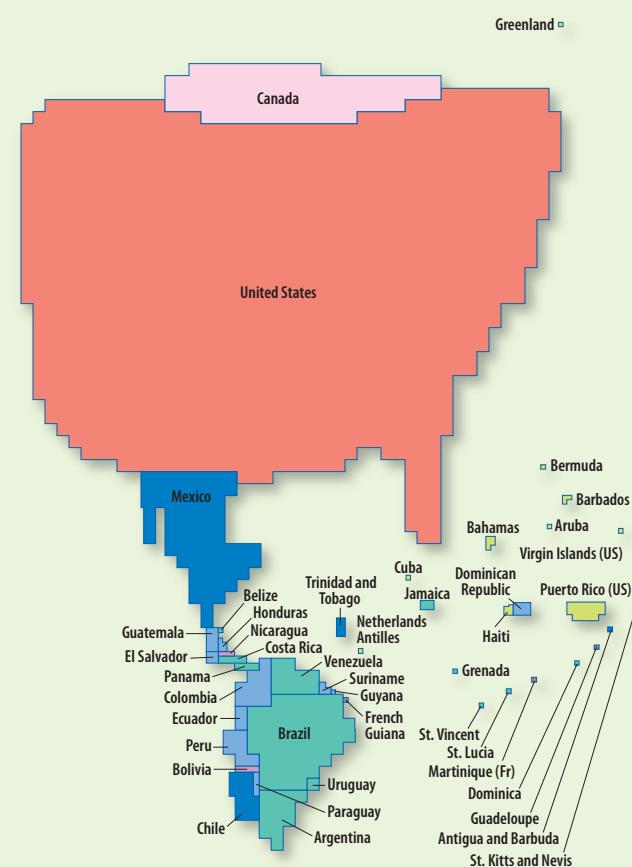
Impact of Economic Growth

Even though about 1 billion people live in poverty today, there has been considerable improvement in recent years. In 1981, for example, 1.5 billion people, or 40 percent of the world population, lived on less than \$1 per day. This figure dropped to 1.2 billion in 1990, or about 28 percent of the world population. By 2001, the number had declined to 1.1 billion, accounting for about 21 percent of the world population.

Figure 17.1 ►

Maps In Motion

See StudentWorks™ Plus or glencoe.com.



GNI Per Capita

\$40,000 +	\$2,500 to \$5,000
\$30,000 to \$40,000	\$1,000 to \$2,500
\$20,000 to \$30,000	\$500 to \$1,000
\$10,000 to \$20,000	under \$500
\$5,000 to \$10,000	no data

Source: The World Bank Development Indicators, 2006

Gross National Income and Gross National Income Per Capita

- If every nation's gross national income were proportional to its total land area, a political map of the world would look like the cartogram in this figure. The colors indicate different levels of national income on a per capita basis and provide another view of a nation's prosperity.

Economic Analysis Which nations have a per capita gross national income similar to that of the United States?



The size of every country is proportional to its gross national income (GNI).
The colors indicate the GNI per capita.



DID You Know?

Economic Development

Economic growth is often uneven. As a result, some countries may be in several stages of development at the same time. For example, many developing nations in Asia went from having no telephones to widespread use of cell phones. At the same time, their populations continue to base other parts of their daily lives on customs and traditions.

primitive equilibrium

first stage of economic development during which the economy is stagnant

countries living on less than \$1 a day by about 2 percent. Economic growth thus is the most effective way of dealing with global poverty.

Concern for Developing Countries

The international community shares humanitarian as well as economic concern for the developing countries. For example, many people in the more developed countries believe that it is their moral responsibility to help those who have less income and wealth than they do.

The concern for the welfare of developing countries is also rooted in self-interest. After all, the developed industrial nations need a steady supply of critical raw materials from the developing nations. In turn, developing countries provide markets for the products of industrial nations.

Political considerations also play a role. Despite the dramatic failure of communism in most countries, various political ideologies wage a continuing struggle for the allegiance of developing countries. Countries that develop strong market economies will not only grow faster, they will also find it both necessary and easier to cooperate with developed countries in world markets. Global economic cooperation, in turn, leads to a more stable political climate.

Reading Check **Interpreting** Why is an understanding of per capita national income important to assess the economic health of nations?

This progress is due largely to the economic growth that has occurred since 1981. In fact, economists found out that a 1 percent increase in the per capita income of developing countries reduces the proportion of people in those coun-

Stages of Economic Development

MAIN Idea Thinking about economic growth as occurring in stages helps us understand economic development.

Economics & You You learned earlier about traditional economies. Read on to find out how this relates to economic development.

Some economists have suggested that developing countries normally pass through several stages of economic development. Others argue that the process is not uniform for all countries. Even if the boundaries between these stages are not always clear-cut, it is helpful to think of economic development as occurring in stages.

Primitive Equilibrium

Economic development starts with a stage called **primitive equilibrium**. It is “primitive” in the sense that the society has no formal economic organization. One example would be the Inuit of the past century you studied in Chapter 2, who shared the spoils of the hunt with other families in the village.

A people—or a country—in primitive equilibrium often has no monetary system and may not be economically motivated toward growth. No capital investment takes place, and the society is in equilibrium because nothing measurable changes. Rules are handed down from one generation to the next, while culture and tradition direct economic decision making.

Transition

The second stage of economic development is a period of transition. It involves breaking away from the primitive equilibrium that exists in a society and moving toward economic and cultural changes. The break may be brief and sudden, or it may take years. A country does not grow economically in this transitional stage, but



old customs begin to crumble. Societies that enter this stage begin to question their traditions and try new patterns of living.

Takeoff

The third stage of development is **takeoff**. This stage is not reached until the barriers of primitive equilibrium have been overcome. A country in the takeoff stage begins to grow more rapidly than before. One reason is that people put customs aside as they seek new and better ways of doing things. In this stage, people also begin to imitate the new or different techniques that outsiders have brought to their country. Still another reason is that an industrialized nation might be providing financial, educational, or military aid. Such assistance helps pay for the things needed to further economic development.

During the takeoff stage, a country starts to save and invest more of its national income. New industries begin to grow rapidly. Industries use new production techniques, and agricultural productivity improves as well.

AP Images

Semidevelopment

The fourth stage is semidevelopment. During this stage, the makeup of the country's economy changes. National income grows faster than population, which leads to higher per capita income. At the same time, the country builds its core industries, spends more heavily on capital investment, and makes technological advances.

High Development

The final stage is high development, where efforts to obtain food, shelter, and clothing are more than successful. Because most people have their basic needs and wants met, they turn their attention to services and consumer goods such as washing machines, refrigerators, cell phones, and video equipment.

The nation no longer emphasizes industrial production. Instead, it increases services and provides more public goods. Mature service and manufacturing sectors are signs of a highly developed economy.

✓ **Reading Check Summarizing** What happens at each stage of economic development?

takeoff third stage of economic development when barriers of primitive equilibrium have been overcome

Stages of Development

Countries may experience several stages of development at the same time. This Mongolian nomad uses solar panels to power the television in her *ger*, or tent.

What stages of development do the solar panels and tent represent?





crude birthrate
number of live births per 1,000 people

life expectancy
average remaining life span in years for persons who attain a given age

zero population growth condition in which the average number of births and deaths balance so that the population size is unchanged

Obstacles to Development

MAIN Idea Numerous obstacles make economic growth in developing countries more difficult than in developed countries.

Economics & You You take graduating from high school for granted. Read on to learn why children in other countries may not be able to attend school at all.

Several possible solutions exist to alleviate the plight of developing countries. However, we first need to take a closer look at some common problems and challenges they face.

Population Growth

One obstacle to economic development is population growth. The populations of most developing countries grow at a rate much faster than the populations of industrialized countries. When a population

grows rapidly, there are more people to feed, and a greater demand for services such as education and health care exists.

One reason for this growth is the high **crude birthrate**—the number of live births per 1,000 people. People in many developing countries are also experiencing an increase in **life expectancy**—the average remaining lifetime in years for persons who reach a certain age. Longer life expectancies, coupled with a high crude birthrate, make it difficult for developing countries to increase per capita GNP.

As a result of the problems posed by population pressures, some countries, such as China, have encouraged lower birth rates and smaller families. Some people even feel that societies should work for **zero population growth (ZPG)**—the condition in which the average number of births and deaths balance.

It is not always possible to restrict population growth, however. In some cultures large families are valued for economic and

Population Growth

This busy street in São Paulo, Brazil, reflects the rapid population growth many developing countries experience.

Why does population growth occur?





personal reasons. In other cultures efforts to disrupt population growth are considered morally wrong for religious reasons.

Natural Resources and Geography

Limited natural resources, such as unproductive land, harsh climates, and scarce energy needed for industry, also can hinder economic growth. Even a limited supply of land becomes critical if a country faces a growing population.

In some cases, countries with limited natural resources can make up for the deficiency by engaging in international trade, as Japan has done. However, if a country is landlocked, such as Paraguay, Nepal, or Chad, trade is more difficult. It is no accident that all of the major economic powers today have long had coastal cities with access to major trade routes.

Disease and Substance Abuse

For many developing nations, health has become a major problem. The HIV/AIDS epidemic has been especially devastating in Africa, with some countries experiencing infection rates as high as 20 percent. Because AIDS generally affects young adults, many families have lost their parents and their **primary** income providers, leaving grandparents and neighbors to raise the children.

In parts of Asia, infectious diseases such as bird flu are a constant concern. When even a minor infestation of this disease occurs, entire stocks of poultry have to be destroyed to prevent its spread. In the areas of Asian and South American nations where illegal drugs are grown and produced, high rates of drug addiction among the local population severely impede the prospects for growth.

Education and Technology

Still another obstacle is a lack of appropriate education and technology. Many developing countries lack the literacy and



Education Science classes, such as this one in a school in Nairobi, Kenya, help countries develop technology skills. *Why is technology important?*

the high level of technical skills needed to build an industrial society.

Many developing countries also cannot afford free public education for children. In those that can, not everyone is able to take advantage of it because children must work to help feed their families.

external debt
borrowed money that a country owes to foreign countries and banks

External Debt

Another major problem facing the developing nations today is the size of their **external debt**—money borrowed from foreign banks and governments. Some nations have borrowed so much that they may never be able to repay these loans.

Today, some developing countries such as the Democratic Republic of the Congo have external debts significantly larger than their GDP. Burundi's external debt is more than twice its GDP, and Liberia's is more than five times larger.



Figure 17.2 ► The Corruption Perception Index

► The corruption perception index shows the degree to which people think corruption exists among their public officials and politicians. The highest score for Iceland indicates that people there think their country has the least corrupt leaders. Chad, with the lowest number, is perceived to have the most corruption.

Economic Analysis *What generalization can you make about economic conditions in the countries with the highest scores?*

Rankings of countries perceived to have the least corruption		Rankings of countries perceived to have the most corruption	
1. Iceland (9.7)	11. Netherlands (8.6)	140. Indonesia (2.2)	150. Tajikistan (2.0)
2. Finland (9.6)	12. United Kingdom (8.6)	141. Iraq (2.2)	151. Angola (1.9)
3. New Zealand (9.6)	13. Luxembourg (8.5)	142. Liberia (2.2)	152. Côte d'Ivoire (1.9)
4. Denmark (9.5)	14. Canada (8.4)	143. Uzbekistan (2.2)	153. Equatorial Guinea (1.9)
5. Singapore (9.4)	15. Hong Kong (8.3)	144. Congo, Dem. Rep. (2.1)	154. Nigeria (1.9)
6. Sweden (9.2)	16. Germany (8.2)	145. Kenya (2.1)	155. Haiti (1.8)
7. Switzerland (9.1)	17. United States (7.6)	146. Pakistan (2.1)	156. Myanmar (1.8)
8. Norway (8.9)	18. France (7.5)	147. Paraguay (2.1)	157. Turkmenistan (1.8)
9. Australia (8.8)	19. Belgium (7.4)	148. Somalia (2.1)	158. Bangladesh (1.7)
10. Austria (8.7)	20. Ireland (7.4)	149. Sudan (2.1)	159. Chad (1.7)

Source: www.transparency.org

default act of not repaying borrowed money

When debts get this large, countries have trouble just paying interest on the loans. As a result, some developing nations have teetered on the brink of **default**, or not repaying borrowed money. Even this outcome is dangerous, however, because a country that defaults on its loans may not be able to borrow again.

Corruption

Government corruption can be an obstacle to economic progress. Corruption can occur on a massive scale, or it can take the form of minor officials requiring modest bribes to get small things done.

Figure 17.2 shows the 20 countries in the world that are perceived to be the least corrupt, along with the 20 considered most corrupt. A casual look at the list reveals

that the countries with the least corruption are more developed than those with the most corruption. Corruption is harmful because it redirects resources into less productive uses. It also makes a few people rich while robbing everyone else.

For example, Nigeria has enormous oil reserves and is one of the 11 members of the Organization of Petroleum Exporting Countries (OPEC). Despite its vast natural wealth, decades of corruption and mismanagement by government officials have left it relatively poor.

War and Its Aftermath

Unfortunately, many of the developing nations of the world—Angola, Afghanistan, Ethiopia, Cambodia, Somalia, and Vietnam, to name just a few—suffered through



bloody civil wars. The immediate impact of war is the devastating loss of lives and property, not to mention the damage to the country's infrastructure.

The aftermath of war can linger for decades. Poland lost virtually all of its *intelligentsia*—its scientists, engineers, and most of its merchant class—to the gas chambers and concentration camps in World War II. The loss of this talent contributed to the slow recovery of the Polish economy after the war, and even hindered its economic development after the fall of communism.

The widespread use of chemical weapons and land mines makes simple activities like farming extremely difficult in many areas. Moreover, many of the people injured by toxic residue and unexploded weapons, such as children playing in fields, were not participants in the war in the first place. The result is that the weapons of war often impede economic development long after the war is over.

Capital Flight

Finally, developing nations also face the problem of **capital flight**—the legal or illegal export of a nation's currency and foreign exchange. Capital flight occurs because people lose faith in their government or in the future of their economy. When capital flight occurs, businesses and even the government often face a cash shortage. At a minimum, capital flight limits the funds available for domestic capital investment.

Private citizens can contribute to capital flight. Suppose that someone in Moscow wants to turn rubles into dollars. The person would first purchase traveler's checks in rubles. Next, the individual would destroy the checks and fly to New York. There the person would declare the checks lost or stolen and get replacement checks in dollars, thereby completing the conversion of rubles into dollars.

✓ **Reading Check** **Recalling** What are the major obstacles to economic growth in developing countries?

capital flight
legal or illegal export
of a nation's currency
and foreign exchange

SECTION

1

Review

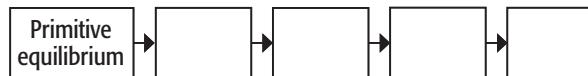
Vocabulary

- 1. Explain** the significance of developing country, primitive equilibrium, takeoff, crude birthrate, life expectancy, zero population growth (ZPG), external debt, default, and capital flight.

Main Ideas

- 2. Explaining** Why is economic development important?
3. Describing Use a graphic organizer like the one below to describe the stages of economic development that many nations experience.

Stages of Economic Development



- 4. Listing** What factors can be obstacles to economic development?

Critical Thinking

- 5. The BIG Idea** Suppose you are an official in charge of economic development in a developing country. Choose two obstacles to economic development that you would address and explain why you would tackle them first.
6. Drawing Conclusions Why is aiding developing countries in the self-interest of the United States?
7. Predicting Imagine that a society is in primitive equilibrium. Provide an example of an event that could bring about change and explain why this might be so.
8. Analyzing Visuals Examine Figure 17.1 on pages 470 and 471. Compare the per capita income of countries in northern Africa with those in Africa south of the Sahara. What do you think accounts for this, and why?

Applying Economics

- 9. External Debt** Many people have suggested debt relief for the poorest of the developing countries. Research debt relief and discuss how it would be applied.



CASE STUDY

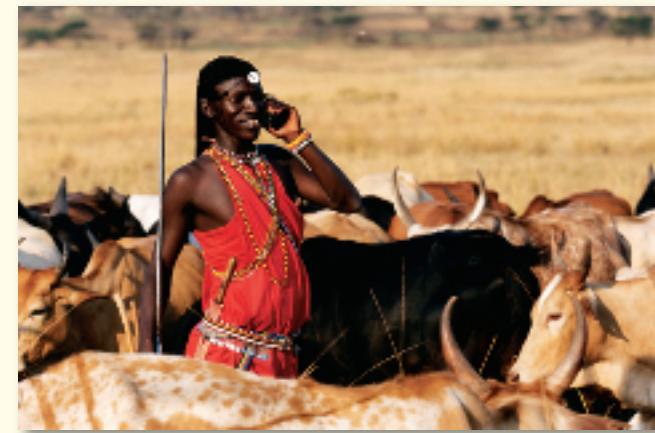
Celtel

Can't Live Without It

In the United States today, many people cannot imagine life without cell phones. The same goes for people living in Africa south of the Sahara, where cell phones often play a high-stakes role. In some areas, such as war-torn Congo, users rely on phones as their only means to keep in touch with family members and friends. Under such dangerous conditions as war, cell phones can truly mean the difference between life and death.

Celtel Boosts African Economy

Throughout most of the 1990s, cell phone service was either nonexistent or very expensive and hard to come by throughout most of central Africa. Then, in 1998, the South African company Celtel launched a mobile communications network in the region. Today it operates in 15 countries and provides more than one-third of the African continent with cell phone service. It has also invested more than \$1.3 billion in African communities.



Celtel had to clear some initial hurdles. Building a communications network is expensive, and many Africans cannot afford to buy the phones, which they usually have to pay for in full. Still, the number of cell phone users has grown from 2 million in 1998 to 117 million in 2005, making Africa the world's fastest-growing cell phone market.

Making a Difference

Access to cell phone service has changed the lives of many people in central Africa. They no longer need to walk miles to talk to a doctor and can more easily communicate with relatives. Celtel's "Celpay" allows people to make banking transactions through their cell phones and to transfer phone minutes to others living in remote villages, where the valuable air time has become a hot commodity. So has battery power. Entrepreneurs provide cell phones for customers to make calls and use car batteries to recharge phones.



Analyzing the Impact

- Summarizing** How has cell phone service changed the lives of many people in remote African villages?
- Inferring** Why would it be difficult to build a cell phone network in Africa south of the Sahara?

SECTION
2

Achieving Economic Development

GUIDE TO READING

Section Preview

In this section, you will learn that developing countries can progress in economic development by finding domestic and international funding and by encouraging regional cooperation.

Content Vocabulary

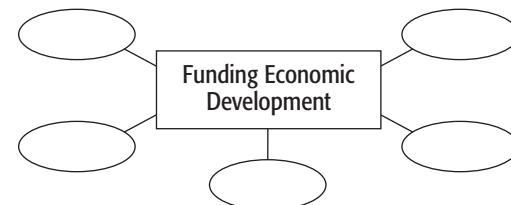
- micro loan (*p. 480*)
- International Monetary Fund (IMF) (*p. 481*)
- World Bank (*p. 481*)
- soft loan (*p. 482*)
- expropriation (*p. 482*)
- free-trade area (*p. 483*)
- customs union (*p. 483*)
- European Union (EU) (*p. 483*)
- euro (*p. 484*)
- ASEAN (*p. 484*)
- cartel (*p. 484*)

Academic Vocabulary

- ethic (*p. 480*)
- duration (*p. 481*)

Reading Strategy

Describing As you read the section, complete a graphic organizer similar to the one below by describing the ways developing countries can finance economic development.



ISSUES IN THE NEWS

—www.dailymail.co.uk

Mitsubishi Investments in Pakistan

Hajime Katsumura, CEO [of] Mitsubishi Corporation, Japan, has said that his company is keen to invest in the agriculture sector of Pakistan as a joint venture and would like to provide modern technology in the dairy sector. . . . “Pakistan is open for investment in all sectors without any discrimination or restrictions on bringing in or taking out capital,” said Zahid Hamid, Minister for Privatization & Investment.

The minister said that the government was ready to facilitate investors to promote both foreign and domestic investment activity in the country. Investors were free to form joint ventures or establish their own businesses with 100% equity. More than 600 multinational companies were successfully operating and making profits in Pakistan, which had become an attractive location for investors. . . . ■



Economic development is important to most countries, but economic development normally requires some type of financing. Sometimes the funding can be generated internally, and sometimes it can be secured from external sources such as foreign governments and foreign investors.

If a developing country has a market economy and the government is politically stable, the country has an even better chance of attracting foreign investment. The search for profits, as you read in the news article above, is a global one that crosses national boundaries.



micro loan small, unsecured loan made primarily to women to help them undertake an income-generating project in a developing country

Funding Economic Development

MAIN Idea Developing countries can fund economic development through savings, international aid and loan programs, and foreign investment.

Economics & You You learned earlier that capital is needed to start or expand a business. Read on to learn how the same principle applies to the developing countries.

The funding for economic development can come from a number of sources. Some sources are internal, while other sources are external, but all are important.

Importance of Savings

Internally generated funds in many cases are the only source of capital for a developing country. To generate these internal funds, an economy must produce more than it consumes.

If a developing country has a market economy, the incentive to save stems from the profit motive. Firms often try to borrow funds for various projects. Banks in turn pay interest rates on savings that are set by the forces of supply and demand. If the demand for money is high, the interest rate will rise, encouraging savings that can be used for investments by firms.

Micro Loans

These three Ugandan sisters used a micro loan to purchase serving trays so that they could start a catering business. **Why are micro loans important to developing countries?**

If a developing country has a command economy, its government may still be able to force saving by requiring people to work on farms, roads, or other projects. However, most command economies do not always mobilize resources to promote economic growth. All too often, resources instead are used for political reasons or personal gain. In addition, forced mobilizations fail to instill long-term incentives or work **ethic** in people.

Microfinance

One of the more successful approaches to economic development in developing countries is the use of **micro loans**. A micro loan is a small unsecured loan, often as small as \$50, made primarily to women who want to undertake an income-generating project. Because more than two-thirds of the GDP in a developing country is produced in activities that are not serviced by banks, the loans provide a way to extend the features of capitalism to the poorest of the poor.

For example, in Africa today, a woman might get the equivalent of a \$50 loan to buy a hybrid goat that produces a higher milk yield. Since the borrower would be too poor to supply collateral, she would get several other women to co-sign the loan in case she defaulted. The loan would have a





International Aid

World Bank loans funded this metal rolling plant in Mombasa, Kenya. **What other agencies provide assistance to developing countries?**

three-month **duration** and require small weekly payments on the principal. To make the payments, the woman would charge a small fee to other villagers to breed her goat with other goats and thus improve the stock of the whole village. Such loans have been enormously popular, and repayment rates in some areas have been as high as 98 percent.

International Agencies

The problems of the developing countries have not gone unnoticed by the developed countries of the world. Two agencies established by the developed nations work directly with developing nations to help solve their problems.

The **International Monetary Fund (IMF)** is an international organization that offers advice to all countries on monetary and fiscal policies. The IMF also helps support currencies so that the countries can compete in an open market and attract foreign investors.

For example, after the Berlin Wall came down and the Soviet Union collapsed, a number of former Soviet-bloc countries wanted to trade their currencies on global exchanges. The IMF provided loans to help with the conversion. This is important because investors must be able to purchase

the currencies of these countries to conduct international trade with them.

The second important international agency is the World Bank Group, more commonly known as the World Bank. The **World Bank** is an international corporation that makes loans and provides financial assistance and advice to developing countries. The World Bank is owned by IMF member nations, but it operates as a separate organization.

The World Bank has undertaken projects to control the desert locust in East Africa. It also has funded projects to develop inland water transportation in Bangladesh, rural transportation systems in Vietnam, and even tax modernization in Kazakhstan.

The International Bank for Reconstruction and Development—part of the World Bank Group—helps developing countries with loans and guarantees of loans from private sources. Many of these loans paid for projects such as dams, roads, and factories. Loans are also made to encourage developing nations to change or improve their economic policies.

Another part of the World Bank Group is the International Finance Corporation (IFC), an agency that invests in private businesses and other enterprises. Finally, the International Development Association

Economics ONLINE

Student Web Activity Visit the *Economics: Principles and Practices* Web site at glencoe.com and click on *Chapter 15—Student Web Activity* for an activity on the International Monetary Fund.

International Monetary Fund (IMF) international organization that offers advice, financial assistance, and currency support to all nations

World Bank international agency that makes loans and provides financial assistance and advice to developing countries



The Global Economy & YOU

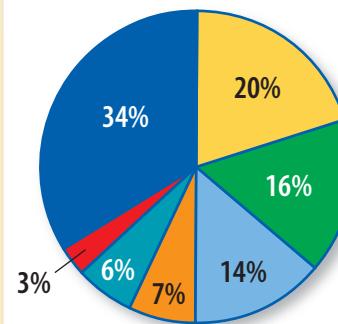


High-Tech Peace Corps

Are you thinking about joining the Peace Corps? If you sign up, don't be surprised to find that you may need some computer skills. The Peace Corps has entered the twenty-first century. In the past, this organization—which provides aid to 183 countries—was mostly about helping farmers, improving infrastructure, and teaching English. Just like the rest of the world, however, the Peace Corp has gone high-tech, thanks in part to the dot-com bust of the late 1990s.

As techies fled Silicon Valley and the failed Internet start-ups in the early 2000s, many of them turned to the Peace Corps for peace of mind. In doing so, they brought new skills to the organization. A new generation of Peace Corps volunteers is now helping developing countries establish computer learning centers and providing support for small business development.

TYPES OF PEACE CORPS AID



- Education
- Health and HIV/AIDS
- Business Development
- Environment
- Other
- Agriculture
- Youth

Peace Corps Volunteers

Gender: 58% female, 42% male

Marital status: 91% single, 9% married

Median Age: 25 years old

Education: 96% undergraduate degree; 13% graduate studies or degrees

Minorities: 16% of volunteers

Source: www.peacecorps.gov

soft loan loan that might never be paid back

expropriation government confiscation of private- or foreign-owned goods without compensation

(IDA) makes **soft loans**—loans that might never be paid back—to the neediest countries. IDA loans are interest-free and may be for periods of 35 or 40 years.

Government Aid Grants

Developing countries can also obtain external funds by borrowing from foreign governments. The United States, Canada, and several countries in Western Europe provide this type of aid.

Political considerations usually play a large role in these grants, so the neediest nations do not always receive the funds. For example, the largest recipient of U.S. government aid is Israel. Pakistan receives financial help from the United States because of its assistance in the war on terrorism.

The former Soviet bloc also gave economic assistance to developing countries. More than half of its aid, however, went to allies such as Cuba, Ethiopia, and Iraq. Like most other foreign aid, it was given to promote political, rather than economic, ends.

Private Foreign Investment

Another way to obtain funds is to attract private funds from foreign investors who might be interested in a country's natural resources. For example, vast oil reserves drew the interest of investors to the Middle East, while copper attracted them to Chile, and mahogany and teakwood to Southeast Asia. In each case, foreign investors supplied the financial capital needed to develop those industries.

If foreign investments are to work, the arrangement must be beneficial to both the investor and the host country. Many investors are unwilling to take major financial risks unless they are sure that the country is politically stable. Developing countries that follow a policy of **expropriation**—the taking over of foreign property without some sort of payment in return—make it harder for all developing nations to attract foreign capital.

Reading Check **Contrasting** How do private foreign investments differ from aid through international agencies?



Regional Economic Cooperation

MAIN Idea Regional economic agreements foster trade and economic growth among member nations.

Economics & You When you have to complete a large project, do you ask others for help? Read on to find out how economic cooperation helps countries.

One way to promote regional economic cooperation is to form a **free-trade area**—an agreement in which two or more countries reduce trade barriers and tariffs among themselves. The free-trade area does not set uniform tariffs for nonmembers.

Several countries could also establish a **customs union**—an agreement in which two or more countries abolish tariffs and

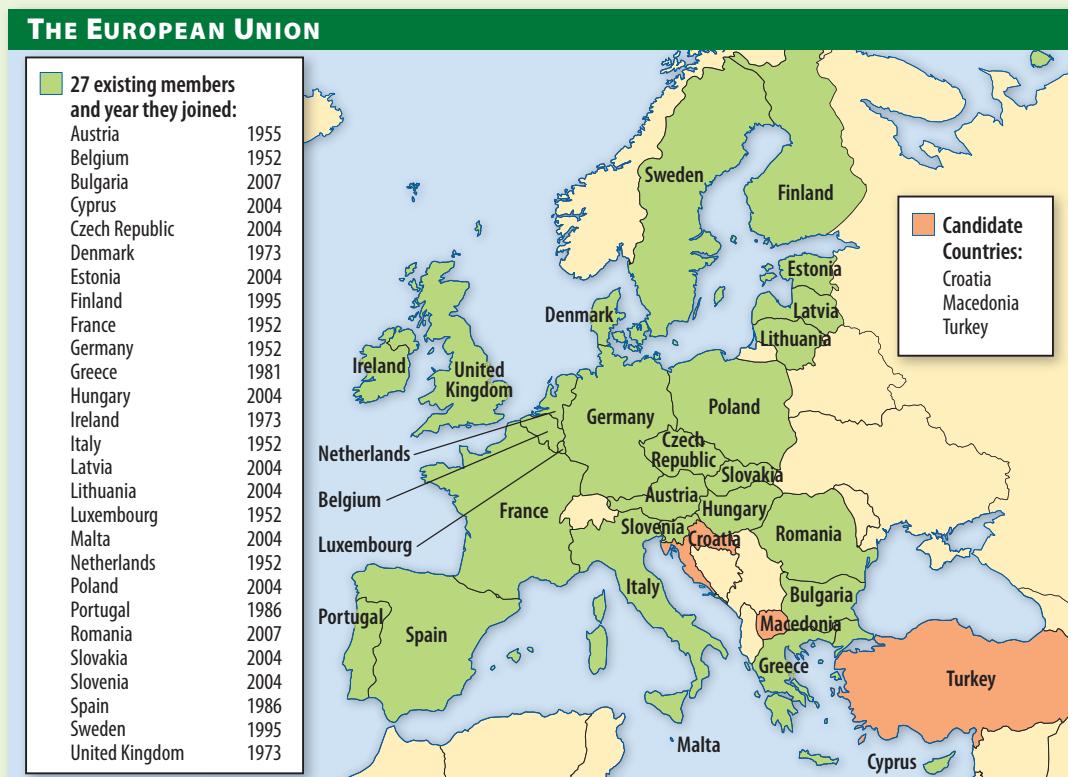
trade restrictions among themselves and adopt uniform tariffs for nonmember countries. The customs union has more uniformity than a free-trade area, so it represents a higher level of economic integration.

free-trade area
group of countries that have agreed to reduce trade barriers among themselves but lack a common tariff barrier for nonmembers

customs union
group of countries that have agreed to reduce trade barriers among themselves and have uniform tariffs for nonmembers

European Union
economic, political, and social union established in 1993 by the Maastricht Treaty as the successor of the European Community

Figure 17.3 ▶ The European Union



- ▶ The 27 members of the European Union, with almost 500 million people, currently make up the largest single market in the world.

Economic Analysis *What are the benefits of membership in the EU?*

Graphs In Motion
See StudentWorks™ Plus or glencoe.com.



euro single currency of the EU introduced in January 2002 and adopted by many member nations

ASEAN group of 10 Southeast Asian nations working to promote regional cooperation, economic growth, and trade

cartel group of sellers or producers acting together to raise prices by restricting availability of a product

of EU member nations hold common passports and can travel anywhere in the EU to work, shop, save, and invest.

The last stage of European integration occurred in 2002 with the introduction of the **euro**—a single EU currency. About half of the member nations have adopted it to replace their national currencies.

ASEAN

The success of the EU has encouraged other countries to try regional cooperation. In 1967 five nations—Indonesia, Malaysia, Singapore, the Philippines, and Thailand—formed the Association for Southeast Asian Nations, or ASEAN. Today, **ASEAN** is a 10-nation group working to promote regional peace and stability, accelerate economic growth, and liberalize trade policies in order to become a free-trade area.

OPEC

In 1960, a number of oil-producing nations formed a **cartel**—a group of producers or sellers who agree to limit the

production or sale of a product in order to control prices. The members of OPEC (Organization of Petroleum Exporting Countries) tried to create the equivalent of a monopoly and push up world oil prices. Since it was organized, higher oil prices have transferred trillions of dollars from industrialized nations to OPEC member countries.

Even with all this financial capital, most OPEC nations have grown slowly by most standards. In Iran, revolution interrupted the development of the domestic economy. In Nigeria, corruption siphoned off most of the oil profits that could have been used for economic development.

High oil prices returned in 2006, but the price increases appeared to be driven more by a strong global demand than by artificially tight supplies caused by OPEC. As a result, OPEC has generally failed to turn the oil cartel into an engine of economic development.

✓ **Reading Check Describing** How do agreements for regional cooperation help member nations?

SECTION

2

Review

Vocabulary

- 1. Explain** the significance of micro loan, International Monetary Fund (IMF), World Bank, soft loan, expropriation, free-trade area, customs union, European Union (EU), euro, ASEAN, and cartel.

Main Ideas

- 2. Identifying** What are two external sources of funds for economic development?
- 3. Describing** What problem is associated with aid grants from foreign nations to developing countries?
- 4. Listing** Use a graphic organizer like the one below to list three examples of regional economic cooperation.



Critical Thinking

- 5. The BIG Idea** What can a country do to encourage economic development?
- 6. Inferring** What are the costs and benefits of regional economic cooperation?
- 7. Synthesizing Information** Why would developing nations be interested in obtaining funding from private sources rather than a government?
- 8. Analyzing Visuals** Look at Figure 17.3 on page 483 and identify the countries that became members of the EU most recently. When did they join?

Applying Economics

- 9. Growth and Development** Provide an example to support the following statement: Economic growth in developing nations is often slowed by the internal political problems and external political goals of industrialized nations.



BusinessWeek NEWSCLIP

As the world's economies become more interdependent, regional cooperation has gained greater importance—even among the most unlikely of partners. In 2006 North Korea, one of the last bastions of communism, cracked open the door to its capitalist neighbor to the south.

Hands Across the DMZ

For decades, there has not been much traffic across the demilitarized zone dividing North and South Korea, where hundreds of thousands of soldiers are on constant alert. But these days, some 200 cars, trucks, and buses cross the border every day.

They're going to the Kaesong Industrial Complex, a dusty outpost that is North Korea's boldest economic initiative in decades. Just an hour north of Seoul, Kaesong is cordoned off from the rest of North Korea by seven-foot-high fences patrolled by squads of soldiers.

Just after 7:00 a.m., Monday through Saturday, dozens of buses from North Korea enter Kaesong, ferrying some 6,000 northern workers to 11 South Korean-owned factories to make shoes, clothing, pots, and other low-tech goods. . . .

The idea behind the effort is simple: North Korea is home to a huge, cheap, and underemployed workforce. South Korea needs a low-wage man-

facturing base to compete with China. By 2012, Kaesong could be home to 725,000 jobs and generate \$500 million in wages annually for the North Korean economy. . . .

North Korea's "Dear Leader," Kim Jong Il, has little choice but to experiment, given the dire condition of the North's economy. . . .

Two Koreas GDP per capita

South
\$20,300

North
\$1,800

Based on purchasing power parity

Source: CIA World Factbook



[S]ince 2002 he has embraced—however grudgingly—tentative economic reforms. . . .

For South Korean companies, Kaesong offers plenty of advantages. North Korean workers at Kaesong earn about \$50 a month, around half the average wage for unskilled workers in China and less than 10% of what South Koreans earn. . . .

Outsourced work for South Korean capitalists may not be exactly what Marx and Engels—or Kim Il Sung (Kim Jong Il's father)—had in mind, but it could be the only hope for Pyongyang.

—Reprinted from *BusinessWeek*

Examining the Newsclip

- 1. Summarizing** How does the Kaesong Industrial Complex meet the needs of both North and South Koreans?
- 2. Making Inferences** Why would North Korea's leadership be opposed to opening up its economy more quickly?



SECTION

3

The Transition to Capitalism

GUIDE TO READING

Section Preview

In this section, you will learn that reforms in the former Soviet Union, China, and many Latin American and eastern European nations have moved these economies toward more capitalistic, market-oriented systems.

Content Vocabulary

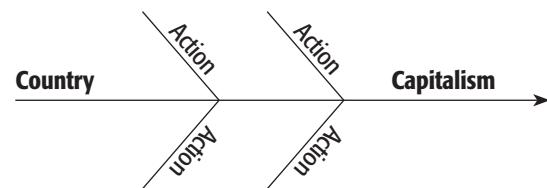
- capitalism (p. 486)
- privatization (p. 487)
- vouchers (p. 488)
- Five-Year Plan (p. 489)
- Gosplan (p. 489)
- collectivization (p. 490)
- perestroika (p. 490)
- Great Leap Forward (p. 490)
- Solidarity (p. 491)
- black market (p. 491)
- capital-intensive (p. 492)
- *keiretsu* (p. 493)
- population density (p. 493)

Academic Vocabulary

- undertaking (p. 488)
- isolationism (p. 491)

Reading Strategy

Describing As you read the section, complete a graphic organizer similar to the one below by selecting a country and describing how it is making the transition to capitalism.



ISSUES IN THE NEWS

South America—Following India or China?

Latin America's challenge can be described in a lot of ways. . . . But the big question facing Latin Americans is: Are they going to emulate India or get addicted to China?

. . . Latin Americans may think that their big choice is between two models of Western capitalism: a European welfare state model and a hyper-competitive U.S. model. But . . . their most important choice is between an India example that focuses on developing human resources and a China syndrome that focuses on selling natural resources. . . . But countries that get addicted to selling their natural resources rarely develop their human resources and the educational institutions and innovative companies that go with that. So after the ore has been mined, the trees cut and the oil pumped, their people are actually even more behind. ■

—The Columbus Dispatch



capitalism
economic system in which private citizens own and use the factors of production in order to generate profits (also see page 38)

As countries develop their economies, **capitalism**, the economic system in which private citizens own and use the factors of production, is spreading around the globe. In fact, when an economy becomes large and complex, capitalism is the most efficient way to organize production and provide the necessary economic incentives.

As countries make the transition to capitalism, the final form of capitalism they adopt will reflect many of their own cultural and social values. As you read in the news story above, countries can follow several different models. That is why so many different faces of capitalism exist in the world today.



Problems of Transition

MAIN Idea Countries in transition to capitalism must learn to abide by the rules of free market economies.

Economics & You Have you ever played a game without knowing the rules? Read on to learn why changing to capitalism can be difficult.

The dominant macroeconomic trend of our lifetime has been the transition of communist and socialist economic systems to capitalism. It has been a transition of epic proportions, and it shows few signs of slowing down.

Even so, the transition is difficult. For one thing, a country making the transition has to convert public property to private ownership. For another, a massive shift of political power takes place during transition. Finally, everyone has to learn to live with the discipline of markets and to abide by a new set of economic incentives.

Why Capitalism?

Simply put, capitalism is the most powerful engine for generating wealth the world has ever seen. Because of capitalism, countries as culturally diverse as Sweden, Japan, the United States, Singapore, Germany, South Korea, and Hong Kong have greatly

increased their productivity and experienced exceptional economic growth.

This growth has improved nearly everyone's standard of living in these countries, and other countries have taken notice. In a world that is becoming increasingly connected by the media and the Internet, people everywhere are aware of—and then begin to want—some of the wealth that capitalism can generate.

In contrast, the collapse of the Soviet Union indicates that communism as an economic system has reached an evolutionary dead end. Pure capitalism can be harsh and may not be attractive to everyone, but in democratic nations, people can modify capitalism to meet more of their economic and social goals. However, there is no guarantee that countries attempting a transition to capitalism will be able to do it smoothly, or that they can do it at all.

privatization
conversion of state-owned factories and other property to private ownership

 **Skills Handbook**
See page R39 to learn about **Formulating Questions.**

Privatization

A key feature of capitalism is the ownership of private property. In order for the transition to capitalism to take place, **privatization**, or the conversion of state-owned factories and other property to private ownership, must be accomplished. Privatization is important because entrepreneurs want to receive rewards for



Privatization
The Dunai Vismu ironworks factory was privatized after the fall of communism and today is the largest of its kind in Hungary. **Why is privatization important?**



voucher certificate that could be used to purchase government-owned property during privatization

undertaking business ventures involving risk. Private property is also important because people take better care of property they actually own.

In Poland, Hungary, and the Czech Republic, this transition was accomplished by using vouchers. **Vouchers** were certificates that could be used to purchase government-owned property. In practice, vouchers were either given to the citizens of a country or sold at very low prices. State-owned companies could then be converted to corporations, and the corporate stock could be auctioned for vouchers. As vouchers were exchanged for shares, ownership of state-owned enterprises transferred to private hands.

Loss of Political Power

Under communism, the Communist Party was the ruling class. When countries changed to capitalism, the party lost much of its political power as a new class of entrepreneurs and capitalists took over.

In countries such as Czechoslovakia, Hungary, and Poland, the Communist Party leaders who were ousted from office lost their power before their country's industry was privatized. In these countries,

the voucher system worked reasonably well to redistribute wealth to new leaders.

In other countries, Communist leaders grabbed a large share of vouchers and thus a large portion of ownership in many privatized companies. In the most blatant cases, some of which occurred in Russia following the collapse of the Soviet Union, the ownership of companies was directly transferred to politicians who were influential during the transition period.

As a result, former political leaders traded their political power for economic power in the form of resource ownership, and the old ruling group simply became the new ruling group. In almost every case of transition, the members of the ruling party had a difficult time actually giving up their power.

Underestimating the Costs

Many countries that want the advantages of capitalism have focused on its benefits, but they have not fully considered its costs. Yet the costs can hinder or even prevent a country's successful transition.

The costs of capitalism during the Great Depression, for example, included instability, unemployment, and social unrest. At

Transition

Countries transitioning to capitalism have to adjust to new costs and incentives. **What are some new incentives?**



Harley Schwadron/Cartoonstock



Russia Today's grocery shoppers in Ekaterinberg, Russia, enjoy a wide range of products in supermarkets. *How does this store compare to grocery stores in the United States?*

that time, the United States did not have the fiscal policies, automatic stabilizers, and social welfare nets needed to lessen the devastation of the Depression. Now that such assistance exists, most economists agree that another Great Depression will not occur in the United States.

The same cannot be said for the countries in transition. They have not yet developed the automatic stabilizers and the social welfare nets that cushion the instabilities of capitalism. During transition, nations will most likely experience the instabilities of early capitalism long before they experience the benefits.

Responding to New Incentives

Finally, people in countries that make the transition to capitalism have to adjust to a whole new set of incentives. They have to learn how to make decisions on their own, take the initiative, interpret prices, and fend for themselves in free markets. Many of these adjustments will be enormous, perhaps even prohibitive. Still, impatience for the end result can be a major obstacle to a successful transition.

Reading Check Summarizing What are the main problems for a nation transitioning to capitalism?

Countries and Regions in Transition

MAIN Idea Different countries have had varying success in their transitions to capitalism.

Economics & You Do you remember adjusting from middle school to high school? Read on to find out why adjusting to a new situation is also difficult for nations in transition.

Despite the transitional problems, nations and regions all over the globe are moving toward capitalism.

Russia

To see why the transition to capitalism has been so difficult for Russia, it helps to understand how the economy was managed during the Soviet era. During this period, the government controlled economic activity with five-year plans. The first **Five-Year Plan**—a comprehensive, centralized economic plan designed to achieve rapid industrialization—was introduced by Joseph Stalin in 1927.

The **Gosplan** was the central authority that devised the plans and directed overall economic activity. It tried to manage the economy by assigning production quotas

Five-Year Plan comprehensive, centralized economic plan used by the former Soviet Union to coordinate the development of industry and agriculture

Gosplan central authority in the former Soviet Union that devised and directed Five-Year Plans



China The People's Republic of China boasts modern manufacturing plants, such as this silk factory in Hotan, Xinjiang. **How do the economic developments of Russia and China differ?**



collectivization forced common ownership of all agricultural, industrial, and trading enterprises used in the former Soviet Union to boost output

perestroika fundamental restructuring of the Soviet economy introduced by Gorbachev

Great Leap Forward China's second five-year plan that began in 1958 and forced rapid industrialization and collectivization of agriculture

to all Soviet industries. Central planning also extended to agriculture with the introduction of **collectivization**—the forced common ownership of all agricultural, industrial, and trading enterprises. Planners then sought to ensure the growth of the economy simply by increasing the quotas given to the farms and factories.

Despite its efforts, central planning eventually failed. The Soviet economy had become too complex and large to be managed by a single planning bureaucracy. Shortages appeared everywhere, and people lacked the incentives to work.

After Mikhail Gorbachev assumed power in 1985, he introduced **perestroika**, the restructuring of the Soviet economy. Under the restructuring, plant managers had more freedom to pursue profits, and small business was encouraged.

Gorbachev's successor, Russian President Boris Yeltsin, accelerated privatization after the fall of the Soviet Union. The government distributed vouchers to citizens so that they could purchase shares of stock in companies being privatized. Eventually Russia opened a stock market, which made the ownership of capital by private individuals a reality in a country that once preached the evils of private property.

Under president Vladimir Putin, privatization began to slow. Under the guise of fighting corruption, Putin used his power to regain centralized control of key energy and mineral industries.

China

The People's Republic of China became a communist economy in 1949. That year the Chinese Communist Party, under the leadership of Mao Zedong, gained control of the country. Over the next few decades, China modeled itself after the Soviet Union, adopting a series of Five-Year Plans to manage its growth.

In 1958 Chinese leaders instituted the **Great Leap Forward**, an attempt to revolutionize industrial and agricultural production almost overnight. This ambitious and radical five-year plan forced farmers off their land to live and work on large, state-owned communal farms.

The Great Leap Forward was a disaster. The agricultural experiment failed, and the economy never came close to achieving the planned degree of industrialization. Other plans followed, but by the late 1970s China finally decided to abandon the Soviet model.



By the early 1980s, the influence of other successful market economies in Asia—especially Hong Kong—was too much for China to ignore. Guangdong Province, one of China's provinces just north of Hong Kong, copied many of the free-market practices of the region and was even allowed to officially experiment with capitalism.

Today China is privatizing industries, introducing market reforms, and otherwise acting in a capitalistic manner. China still has a long way to go, but the progress made so far is remarkable. China has become one of the world's major economic powers, a transition made possible because of its willingness to replace communist ideology and control with capitalistic practices.

Latin America

In the past, many Latin American countries followed a path of economic development that combined socialism and **isolationism**. Chile, however, took major steps to foster the growth of capitalism when it privatized airlines, telephone services, and utilities. The country even used the billions deposited in its pension funds to supply capital to new entrepreneurs. As a result, it now exports copper, paper and pulp, fruit, and chemicals.

Argentina has similarly embarked on a program to remove government from the everyday business of running the economy. The government has sold state-owned oil fields, petrochemical plants, and a number of other businesses to private companies.

Eastern Europe

The nations of Eastern Europe, especially those that were unwilling members of the former Soviet bloc, were eager to shed communism and embrace capitalism. By 2007 ten of these nations had joined the European Union as full-fledged members.

The struggle for freedom began in Poland with **Solidarity**, the independent and sometimes illegal labor union established in 1980. Solidarity was influential in securing a number of political freedoms

in Poland. Eventually, the Communist party lost power, and interest in capitalism grew. In 2004 Poland joined the EU.

Hungary also made a successful transition to a market economy. It was considered the most "Western" Communist bloc country, with a thriving **black market**—a market in which entrepreneurs and merchants sold goods illegally. Hungary's

Solidarity
independent Polish labor union founded in 1980 by Lech Wałęsa

black market
market in which economic products are sold illegally

CAREERS

Urban and Regional Planner

The Work

- * Develop long- and short-term plans for the growth and revitalization of urban, suburban, and rural communities
- * Help local officials make decisions concerning social, transportation, economic, and environmental problems
- * Promote the best use of a community's land and resources for residential, commercial, institutional, and recreational purposes
- * Ensure that developers follow zoning codes, building codes, and environmental regulations



Qualifications

- * Strong analytical, spatial-relationship, and problem-solving skills
- * Master's degree from an accredited program in urban or regional planning, urban design, or geography
- * College courses in architecture, law, earth sciences, demography, economics, finance, health administration, geographic information systems, and management
- * Experience with computer programming and statistics

Earnings

- * Median annual earnings: \$53,450

Job Growth Outlook

- * Average

Source: *Occupational Outlook Handbook, 2006–2007 Edition*

**Figure 17.4**

Economic Systems and Economic Success

- Countries that have had longer experience with capitalism also have higher per capita GDPs.

Economic Analysis *Why is Russia's per capita GDP lower than that of Hungary or Poland?*

ECONOMIC SYSTEMS AND PER CAPITA GDP		
Country	Economic System	Per Capita GDP
United States	Capitalistic	\$41,800
Hong Kong	Capitalistic	\$32,900
Japan	Capitalistic	\$31,500
Sweden	Capitalistic	\$29,800
Singapore	Capitalistic	\$28,100
Korea, South	Capitalistic	\$20,400
Czech Republic	Capitalistic	\$19,500
Estonia	Capitalistic	\$16,700
Hungary	Capitalistic	\$16,300
Slovakia	Capitalistic	\$16,100
Lithuania	Capitalistic	\$13,700
Poland	Capitalistic	\$13,300
Latvia	Capitalistic	\$13,200
Argentina	Transition	\$13,100
Chile	Transition	\$11,300
Russia	Transition	\$11,100
Mexico	Capitalistic	\$10,000
China	Transition	\$6,800
Korea, North	Command	\$1,700

Source: CIA 2006 Factbook

Note: Comparisons are on a Purchasing Power (PPP) basis.

capital-intensive production method requiring relatively large amounts of capital relative to labor

experience with these markets helped ease the transition to capitalism. It too became a full member of the EU in 2004.

Finally, the Czech and Slovak Republics, along with the Baltic states of Estonia, Latvia, and Lithuania, also made great strides toward capitalism following the collapse of the Soviet Union. These countries, along with Slovenia, were all granted admission to the European Union in 2004. All of these countries thus completed one of the more remarkable transitions of economic systems in history—going from communism to capitalism in a relatively short time.

Reading Check **Comparing** How were the transitions similar and different for Russia and the Eastern European countries?

Other Faces of Capitalism

MAIN Idea A number of nations have developed successful free market economies.

Economics & You You are familiar with capitalism in the United States. Read on to learn how it can differ in other countries.

Some former socialist or communist countries are still making the transition to capitalism. Other countries have had successful capitalist economic societies for some time. This is one reason that so many other countries are trying to make the transition. As **Figure 17.4** shows, capitalistic countries have much higher per capita incomes than other countries.

Japan

Japan, like the United States, has a capitalist economy based on markets, prices, and the private ownership of capital. There are several reasons for Japan's success. One reason is that Japan has a loyal and dedicated work force. At many companies, employees even arrive early for work to take part in group calisthenics and meditation with the intent on making their day more productive.

Another reason is the ability and willingness of the Japanese to develop new technologies. Because of its small population, Japan has worked to boost productivity by developing methods that are **capital-intensive**—using a large amount of capital for every person employed—rather than labor-intensive. As a result, Japan is recognized as the world leader in the area of industrial robots.

The feature that sets Japan apart from the United States is the degree to which Japan's government is involved in the day-to-day activities of the private sector. The country's Ministry of International Trade and Industry (MITI), for example, is a government body that identifies promising export markets. The ministry then provides subsidies to industries to make them competitive in those areas.



Despite Japan's successes, it experienced stagnation for most of the 1990s. Part of the reason is that most large Japanese firms belong to a *keiretsu* (kay • reht • soo), a tightly knit group of firms governed by an external board of directors. The role of the *keiretsu* is to ensure that competition does not threaten individual firms. This group also supervises potential competitors, which harms economic growth. A similar agreement in the United States among competing firms would be illegal under our antitrust laws.

Modest economic growth returned in 2004, but the close relationship between government and industry makes it difficult for incremental change, one of the features of capitalism, to take place. This is an ironic turn of events because the world looked to Japan as the very model of growth in the 1980s. Today Japan turns to the United States for guidance on restructuring so that it can resume its previous growth.

South Korea

One of the most successful nations in Asia is South Korea. In the mid-1950s, after it became divided from North Korea, South Korea was one of the poorest countries in Asia. It needed to rebuild an economy torn up by war. The country also had the highest **population density**—number of people per square mile of land area—in the world.

The South Korean government began by opening its markets to world trade. At first, the government focused on only a few industries. This allowed its people to gain experience producing and exporting for world markets. Businesses in the South Korean economy began to produce inexpensive toys and consumer goods. As they became skilled in production and exports, businesses next moved into textiles such as shirts, dresses, and sweaters. They then invested in heavy industry, such as shipbuilding and steel manufacturing.

keiretsu

independently owned group of Japanese firms governed by an external board of directors in order to regulate competition

population density

number of people per square mile of land area



South Korea

Electronics manufacturing such as in this Samsung plant has helped South Korea become a highly developed country. **What were initial stumbling blocks for South Korea?**



Taiwan Taipei, the capital of Taiwan, is home to this Ford Motor factory.
What issues might slow future growth for Taiwan?



Today, South Korea is a major producer of consumer and electronic goods such as home appliances and televisions. The country also has become a leading producer of automobiles. The South Korean experience shows that capitalism can change a badly war-damaged economy into a well-developed, highly industrial one in just a few generations.

Singapore

Singapore is a small island nation about 3.5 times larger than Washington, D.C. It has a per capita GNP slightly more than two-thirds of that of the United States. The lure of generous tax breaks, government subsidies, and government-sponsored training of employees has attracted thousands of multinational firms to Singapore. Efforts to develop its own technologies through spending on research and development account for a significant part of its strong economic growth.

The government of Singapore has focused on a few select industries, including telecommunications services, software, and biotechnology. The government has spent millions on laboratories, attracting

top scientists from all over the world. The biotechnology industry has scored some original successes, one of which is the transfer of firefly genes to orchids to make them glow in the dark.

Taiwan

The Republic of China, also known as Taiwan, is located off the coast of the much larger People's Republic of China. The population of Taiwan is about 23 million, and the per capita GNP is almost two-thirds of that of the United States.

Planning has always been a feature of the Taiwanese economy, with the government trying to identify those industries most likely to grow in the future. Most of these plans target high-tech industries such as telecommunications, consumer electronics, semiconductors, precision machinery, aerospace, and pharmaceuticals.

Taiwan was one of the early economic powers in Asia, but some experts have warned that the centralized planning process will hamper future economic growth. Another concern is the looming presence of the People's Republic of China, which regards Taiwan as a "renegade province"



and vows eventual unification. Despite its early start, the per capita GNP in Taiwan has fallen behind those of Hong Kong and Singapore.

Sweden

Sweden, now a mature industrial nation, was once regarded as the “socialist state that works.” The reputation was apt at the time, because Sweden provided a broader range of social welfare programs for its citizens than did any other noncommunist country. The Swedish economy—with its generous maternity, education, disability, and old-age benefits—was thought to be the model of European socialism.

Social benefits were expensive, however, and to pay for them tax receipts were about 50 percent of GDP in the mid-1970s. In addition, some marginal tax brackets reached 80 percent, meaning that a person who earned an additional \$100 would keep only \$20. Many individuals even left the country to avoid high taxes. When tennis

star Bjorn Borg was at the peak of his career, for example, he resided outside of Sweden to avoid paying high taxes.

Eventually the heavy tax burden, the costs of the welfare state, and massive government deficits cut into Sweden’s economic growth and led to the defeat of the Socialist Party. By 1991 a government committed to a free market economy was firmly in place. It reduced the role of the public sector, lowered taxes, and privatized many government-owned businesses.

Today Sweden features a mix of high-tech capitalism and liberal welfare benefits. The generous welfare system is thought to be the reason why Swedish workers report in sick more often than other European workers. The taxes required to support the welfare system also have kept its GDP per capita below that of its closest neighbors, Denmark, Finland, and Norway.

✓ **Reading Check** **Explaining** How did Japan, Singapore, and South Korea manage to become successful?

SECTION

3

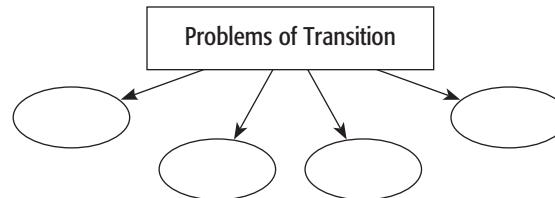
Review

Vocabulary

- 1. Explain** the significance of capitalism, privatization, vouchers, Five-Year Plan, Gosplan, collectivization, perestroika, Great Leap Forward, Solidarity, black market, capital-intensive, *keiretsu*, and population density.

Main Ideas

- 2. Listing** Use a graphic organizer like the one below to list four problems faced by economies in transition.



- 3. Describing** How do economies in transition handle privatization?

- 4. Explaining** What are the contrasting approaches to economic growth in Taiwan and China?

Critical Thinking

- 5. The BIG Idea** Evaluate the progress of Poland, Russia, and South Korea in moving toward a market system.
- 6. Drawing Conclusions** Why would a developing nation want to choose capitalism?
- 7. Making Connections** Suppose you are visiting a nation in Central Asia. What questions would you ask local officials to determine whether they are successfully moving toward a market economy?
- 8. Analyzing Visuals** Compare the photo of a Russian supermarket on 489 with that of a North Korean grocery store on page 37. How do the two stores reflect the differences in economic systems?

Applying Economics

- 9. Economic Growth** Why would capital equipment and other property last longer when it is privatized rather than collectively owned?



Profiles in Economics



Karl Marx's ideas were so radical during his time that he was persecuted by authorities. In 1849 he fled to London, where he began a life of exile and later died in poverty. Still, Marx was named the "Greatest Philosopher of All Time" in a BBC poll in 2005.

Karl Marx (1818–1883)

- published *The Communist Manifesto* in 1848
- his ideas inspired communist revolutions

The Communist Manifesto

Karl Marx was an economic historian and social scientist who earned his degrees at the University of Berlin. Because of his radical views, however, he could not get a teaching position in Germany and eventually moved to the United Kingdom.

Marx is best known for *The Communist Manifesto*, published in 1848, and *Das Kapital*, the first volume of which was published in 1867. In these works, Marx asserted that "the history of all hitherto existing society is the history of class struggles," and in each era, one class was pitted against another. Marx believed that the oppressed of his day were the proletariat—people who must work for others because they have no means of production of their own. Their oppressors were the bourgeoisie, or capitalists—people who own the means of production.

Ideas to Spread the Wealth

Marx argued that labor was exploited in a capitalist society, and that capitalists unfairly kept surplus value—the difference between wages and market value of workers' output—as profits. To fight unequal wealth, the proletariat should violently overthrow the ruling class: "Working men of all countries, unite!"

During the transition from capitalism to communism, Marx thought that the proletariat would first have to depend on a strong government—a "Dictatorship of the Proletariat." Eventually this would be replaced by a classless or communal society, with no need for a government. People would produce to the best of their abilities and consume to the extent of their needs.

The ideas of Marx served as the basis for communist revolutions around the world in the early to mid-1900s. Since then, most communist governments have collapsed, and today only a few communist countries remain.

Examining the Profile

- Analyzing** Why did Marx believe that workers would be interested in staging a revolution and overthrowing the ruling class?
- Making Inferences** Do you believe class struggles are occurring in the world today? Explain your answer.



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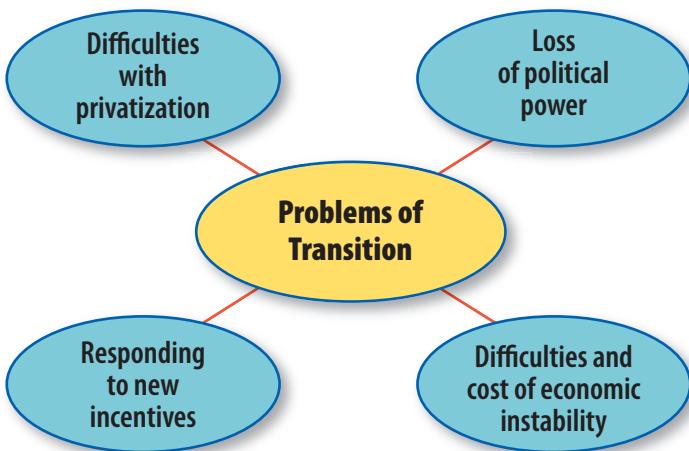
- **Stages of Economic Development** Countries usually go through several stages of economic development, although the boundaries between these stages may overlap.



- **Funding Economic Development** Countries that need to develop their economies have a variety of funding sources available to them.

Internal Funding Sources		External Funding Sources		
Saving	Microfinance	International Agencies	Government Aid Grants	Private Foreign Investments
<ul style="list-style-type: none"> Profit motive as incentive Generates financial capital 	<ul style="list-style-type: none"> Small unsecured loans for new businesses No bank loans required 	<ul style="list-style-type: none"> IMF: advice on fiscal policies and currency support World Bank: financial assistance 	<ul style="list-style-type: none"> Grants and loans from foreign governments Usually linked to political alliances 	<ul style="list-style-type: none"> Foreign investors develop specific industries Must be beneficial to investor and host country

- **Problems of Transition** While capitalism provides a remarkable degree of economic growth, making a successful transition to capitalism can be difficult.



Assessment & Activities

Review Content Vocabulary

Write the key term that best completes the following sentences.

- | | |
|----------------------|-----------------------|
| a. capital flight | f. expropriation |
| b. capital-intensive | g. external debt |
| c. cartel | h. micro loan |
| d. crude birthrate | i. population density |
| e. customs union | j. takeoff |

1. A(n) _____ is a formal arrangement to limit the production of a product.
2. A _____ helps people in developing countries obtain minimal funding to start small businesses.
3. A(n) _____ is a cooperative arrangement among nations that sets uniform tariffs for nonmembers.
4. A developing country may have a very high _____, contributing to rapid population growth.
5. When _____ becomes too large, countries have difficulty paying the interest.
6. The third stage of economic development is the _____.
7. The problem of _____ occurs when corrupt officials take money out of the country and deposit it abroad.
8. When _____ takes place, it is more difficult for developing nations to attract foreign capital.
9. The number of people per square mile of land is a measure of _____.
10. In _____ industries, a large amount of capital is used for every person employed in manufacturing.

Review Academic Vocabulary

Use each of the following terms in a sentence that reflects the term's meaning in the chapter.

- | | |
|----------------|------------------|
| 11. proportion | 14. duration |
| 12. primary | 15. undertaking |
| 13. ethic | 16. isolationism |

Review the Main Ideas

Section 1 (pages 469–477)

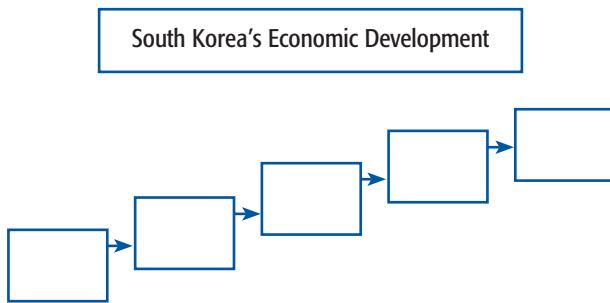
17. **List** two reasons why there is concern for the plight of developing countries.
18. **Describe** the stages of economic development.
19. **Explain** why the size of the population can create a problem for a developing country.

Section 2 (pages 479–484)

20. **Describe** how the World Bank assists developing countries.
21. **Explain** how a developing country can attract foreign capital.
22. **Identify** the benefits of membership in the European Union.

Section 3 (pages 486–495)

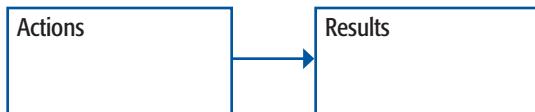
23. **Explain** why countries would want to make a transition to capitalism.
24. **Describe** how Latin American countries have approached the transition to capitalism.
25. **Identify** the steps in South Korea's economic development by using a graphic organizer like the one below.



Critical Thinking

26. **The BIG Ideas** What do you think would happen if industrialized nations and international agencies chose to withdraw their support from developing nations?

- 27. Synthesizing** What actions can the United States take to help the developing countries of Latin America? Use a graphic organizer similar to the one below to describe the actions and the possible results.



- 28. Drawing Conclusions** What economic and political conditions in developing countries encourage foreign investment?
- 29. Making Generalizations** Studies indicate that, in general, landlocked nations tend to have lower per capita income levels than surrounding nations that are bordered by oceans and seas. Why do you think this is the case?
- 30. Predicting** How might continued economic growth in Asia affect the United States?
- 31. Drawing Conclusions** Why do many U.S. companies think their Chinese competitors have an unfair advantage?
- 32. Drawing Conclusions** The Communists promised people that their system would lead to workers' parades throughout the world, but by the early 1990s, most communist systems and their command economies in Eastern Europe had collapsed. Why do you think communism failed?
- 33. Drawing Conclusions** How has Sweden's transition from socialism to capitalism helped promote economic growth?

Analyzing Visuals

- 34.** Look at the photo on page 474 of Tokyo, Japan. Describe the photo and explain how it reflects rapid population growth. Then consider if this photo reminds you of similar places. Now look at the photo of Times Square in New York City on page 412. How are the two images similar? How are they different?

Thinking Like an Economist

- 35. Critical Thinking** What advice would you give a developing Latin American nation that was trying to decide whether to pattern its economic development strategy on India or China? Explain your answer.

Writing About Economics

- 36. Expository Writing** News media often report on the economic problems of developing nations. For one week, keep a journal of all the news stories you see and read about. Then complete the following steps.
- Create a list with the countries in one column and their problems in a second column.
 - Using the information you collected, write a plan detailing how the United States could assist in alleviating some of the economic problems of a specific country. Be sure to support your proposal with statistics, facts, quotes, and historical events.
 - Present your conclusions to the class.

Applying Economic Concepts

- 37. Growth and Development** How do you think the economic growth of developing countries will affect you and your family in the future?
- 38. Economic Development** On their way to high development, many developing countries may go through several stages of economic development at the same time. Select three developing countries. In a table similar to the one below, identify the stages of economic development for each. Explain your reasons.

Country	Stages	Reason