# Human Face of Poverty: Exploring Causes and Solutions
## Lesson 2: Neoliberalism

**Standards Addressed by Lesson:** **CIVICS** Standard 3.3 Students understand the domestic and foreign policy influence the United States has on other nations and how the actions of other nations influence politics and society of the United States. **ECONOMICS** Standard 2.3 Students understand that government actions and policies, including taxes, spending, and regulations influence the operation of economies. (d) Standard 3.1 Students understand that the exchange of goods and services creates economic interdependence and change (a – d). (a,e) **HISTORY** Standard 4.2 Students understand how economic factors have influenced historical events. (d,e) Standard 4.3 Students understand the historical development and know the characteristics of various economic systems (b,c,d).

**Objectives of Lesson:** To expose students to some basic concepts of global economics and encourage them to think critically about the strengths and weaknesses of the current, dominant model.

**Instructional Strategies:** Brainstorm

**Vocabulary:** Neoliberalism, tariffs, quotas, subsidies, privatization, free trade

**Suggested Time:** Between 50 and 60 minutes

**Needed Materials:** Newsprint, markers, props

**Attachments:** A. The Neoliberal Recipe/ Econ 101

## Lesson Outline

### Introduction to Lesson:

Activities in this lesson plan can either be incorporated into Lesson 1 on Globalization (depending on class time and/or grade level) or be given as a separate class. The educator should explain to students that the goal of the next 50 – 60 minutes is to introduce and explore the concept of neoliberalism and to develop an understanding of what it means and how it has impacted Latin American countries.

Remind the group that you are not an expert on these issues and are hoping that students will also offer their expertise, insight, perspectives. This workshop is meant to be interactive and participatory.

Before beginning, it is important to remember that when trying to understand these concepts and what they mean for Latin America and especially Guatemala, it is important to remember there is no black or white. As in any system of economics, there are strengths as well as weaknesses. No economic system exists in a vacuum but is impacted and influenced by external factors.

## Activities

### <u>Activity 1: Brainstorm Neoliberalism</u>

First ask students what they know about "neoliberalism" and put their thoughts up on newsprint. Some points to make about neoliberalism if they don't come up in class:

- This is an economic theory that began to take hold in the early 1980s as increased production in the global north prompted businesses to look toward developing countries to find external markets to which to sell their surplus.
- Government limits its role in the economy in order to foster market-led growth and development, which is to say that it doesn't offer protection to its industries. Notable exceptions are the U. S. and the European Union which do offer price supports, especially to large agricultural producers.
- Neoliberalism posits that the free market system will provide prosperity to the greatest number of people. Growth in the private sector will theoretically create jobs and benefits will trickle down to all members of society.
- The underlying principle behind this model is that of "comparative advantage." In presenting this principle in the early 19th century, David Ricardo argued that each nation should produce those goods that it can produce the most efficiently relative to other nations. (For example, Guatemala produces bananas more efficiently than the United States, and the United States produces hamburger more efficiently than Guatemala. Therefore, the U.S. should focus its economic energy on producing meat and buy its bananas from Guatemala; and Guatemala should focus on producing bananas and buy its hamburger from the United States.)
- The implementation of the neoliberal economic model also relies on the privatization of many services generally considered "public," e.g. water, telephone, utilities, etc.
- The completion of neoliberalism creates a market in which "free trade" can occur.

### <u>Activity 2: Recipe for Neoliberalism</u>

Break the students up into three groups and explain that they will be discussing what the "recipe" for a neoliberal economy is (Attachment A). Give each group a "recipe" card to discuss with props for skit. Give them 25 minutes to read and discuss their "ingredient" and come up with a skit using the props to explain how this "ingredient" is reflected in Mexico. At the end of the 25 minutes, have each group present what their "ingredient" is followed by their skit.

**Group One: Trade Liberalization**

- *Trade liberalization*: reduced trade barriers such as tariffs and quotas. Tariffs are taxes placed on imported goods and quotas limit the amount of imported goods that can come into the country. This would include removing protections on new industries.

***Props*** (These are suggested props, however the educator may come up with some of his or her own.): cardboard cutout of Mexican corn cob, sombrero for Mexican farmer, bag of U.S. corn, mustache to represent Mexican government, and cardboard cut out of a few giant tacks to represent an import tax (tariffs).

***Scenario to play out***: What does this mean for Mexico? To protect its corn farmers, the Mexican government might impose a tariff on foreign corn in order to make it difficult for U.S. corn producers to export their corn to Mexico. The Mexican government can limit importation by placing tariffs (import taxes) on the U.S. corn or placing quotas on it which determine how much corn the U.S. can export to Mexico. As a result, Mexican corn producers do not have to worry about competing with foreign producers; they do not have to worry that a Mexican consumer might buy the U.S. corn instead of their own. Neoliberalism requires that governments remove these protections as they impede the flow of free trade. These provisions are contained in trade agreements, e.g. NAFTA.

**Group Two: Removal of State Subsidies**

- *Remove state subsidies* on goods and services. Subsidies are resources, money from the government to a certain sector of the economy. For example, corn farmers might receive a guaranteed price for their corn, low-cost fertilizers, and free farming equipment. Subsidies also reduce the cost of health care services and education because the government may pay for part of these costs. Under neoliberalism, the government would remove all this support.

***Props***: mustache to represent Mexican government, cardboard cut outs of a dollar sign, a bag of money, a hoe for the farmer, seeds.

***Scenario to play out***: What does this mean for Mexico? State subsides are a form of assistance from the government. Using the example of corn farmers, under the old system, corn farmers might receive seeds, fertilizers, pesticides at a reduced cost. Other subsidies might include low interest credit to help farmers. They might get subsidies or economic support in other forms, e.g., the government might pay them a certain amount for their corn that was destroyed by drought. Neoliberalism demands the government save money by removing this support to farmers, and thus not give them an unfair advantage over farmers in other countries. (Remember the exceptions in the U.S. and the E.U.)

**Group Three: Privatization**

- *Privatization*: the selling off of state-owned enterprises such as oil, phone, electricity (Theory is that private capital will more efficiently run industries).

***Props***: mustache to represent Mexican government, light bulb to represent electrical industry, cardboard cut outs of a dollar sign.

***Scenario to play out***: What does this mean for Mexico? The government owns the electrical industry, but it is expensive to run this industry. The industry is also using old, inefficient technology. Under neoliberalism, the government would sell the industry to an individual or company. This gives the government one-time revenue from the sale of the industry, and hypothetically results in the new private owner running the industry more efficiently. What often happens, however, is that the cost of electricity (or other privatized services) becomes more expensive. Another risk is that the industry is sold to a foreign company or investors.

After each group has completed their skit, the educator should explain the three other components of neoliberalism:

- *Deregulate*-eliminates price limitations on basic commodities and allows market to determine prices.
- *Ease or eliminate restrictions on foreign investment*-allow foreign ownership of certain industries; offer tax breaks or incentives; ease workers' rights and environmental restrictions, to name but a few examples.
- *Devalue currency*-make each unit of currency, e.g. the peso, worth less. If we think of this in terms of wages, the factory probably wouldn't increase wages to its workers so, in effect, it is paying less. The worker earns the same number of pesos but it takes more pesos to buy a gallon of milk, etc.

**Activity 3: Evaluating Neoliberalism**

Place two pieces of newsprint up on the board. One labeled Strengths, the other Weaknesses. Open it up to the group asking them to think about the skits they saw and come up with a few strengths and weaknesses of the model.

- Strengths might include: increased competition, greater efficiency, infrastructure improvements, lower prices and increased foreign investment.
- Weakness might include: widening wealth disparities, externalities (i.e. environmental degradation, poor labor standards), "race to the bottom."

***Potential problems with the free market system educator should point out:***

- Developing nations rarely can negotiate trade agreements from a position of strength.
- Unfair competition: monopolies can manipulate prices and wages to their advantage, often hurting consumers and/or workers.
- Under-provision of public goods: the free-market does not provide things like roads, education, public security, or justice systems because once produced these goods and services are freely available for use by everyone.
- Externalities: Producers do not internalize all of the costs of production and pass them on to society in the form of poor labor conditions or environmental pollution.
- An unchecked market results in wealth disparities and perpetuation of economic oppression.

- This situation often results in the "forced economic migration" of workers from developing nations to the U.S. and Europe.

**Helpful Hints / Comments from Previous Facilitators:** If the grade level and/or background of the students are not advanced enough to have them break up into groups to illustrate the neoliberal recipe, the concepts can also be illustrated by having the educator ask for volunteers and play out the different scenarios in front of the class.

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## Attachment A: The Neoliberal Recipe

**1. LIBERALIZE TRADE**
- Government does not regulate

**2. REMOVE STATE SUBSIDIES**
- Government does not help

**3. PRIVATIZE**
- Government does not own services

**4. DEREGULATE**
- Government does not limit prices

**5. EASE OR ELIMINATE RESTRICTIONS ON FOREIGN INVESTMENT**
- Government does not restrict foreign companies

**6. DEVALUE CURRENCY**

## Econ 101

**Neoliberalism:** This is an economic theory that began to take hold in the early 1980s, as increased production in the global north prompted businesses to look toward developing countries to find external markets to which to sell their surplus. Neoliberal theory demands that government limit its role in the economy in order to foster market-led growth and development. Neoliberalism posits that the free market system will provide prosperity to the greatest number of people. Growth in the private sector will theoretically create jobs and benefits will trickle down to all members of society.

The underlying principle behind this model is that of comparative advantage. In presenting this principle, David Ricardo argued that each nation should produce those goods that it can produce the most efficiently relative to other nations. For example, Guatemala produces bananas more efficiently than the United States, and the United States produces hamburger more efficiently than Guatemala. Therefore, the U.S. should focus its economic energy on producing meat and buy its bananas from Guatemala; and Guatemala should focus on producing bananas and buy its hamburger from the United States.

**Recipe for a Neoliberal Economy** (* denotes concepts that DJPC has successfully taught to high school students in the past. Other concepts have thus far only been discussed in adult workshops.)

- **Liberalize trade*: reduce trade barriers such as tariffs and quotas. This would include removing protections on new industries. What does this mean for Mexico? To protect its corn farmers, the Mexican government might make it difficult for US corn producers to export their corn to Mexico through imposing a tariff on foreign corn. The Mexican government might do this by placing tariffs (import taxes) on the US corn or they might place quotas on them which determine how much corn the US can export to Mexico. As a result, corn producers do not have to worry about competing with other foreign producers; they do not have to worry that a Mexican consumer might buy the US corn instead of their own. Neoliberalism requires that governments not provide these protections as they impede the flow of free trade.

- **Remove state subsidies* on goods and services (e.g. subsidies to help corn farmers, or subsidies to services like health care and education). What does this mean for Mexico? State subsides are sort of like assistance from the government. Using the example of corn farmers, under the old system, corn farmers might receive seeds, fertilizers, pesticides at a reduced cost. Other subsidies might include low interest credit to help farmers. They might get subsidies or economic support in other forms, like the government might pay them a certain amount for their corn that was destroyed by drought. Neoliberalism demands the government save money by not providing this support to farmers, and thus not give them an unfair advantage over farmers in other countries.

- **Privatize*: the selling off of state-owned enterprises such as oil, phone, electricity (theory is that private capital will more efficiently run industries). What does this mean for Mexico? The government owns the electrical industry, but it is expensive to run this industry. The industry is also using old, inefficient technology. Under neoliberalism the government would sell the industry to an individual or company. This gives the government additional revenue from the sale of the industry, and hypothetically results in the new private owner running the industry more efficiently.

- *Deregulate:* eliminate price limitations on basic commodities and allow market to determine prices.

- *Ease or eliminate restrictions on foreign investment:* government does not adopt measures to curb or control investment by foreign companies.

- *Devalue currency*: government reduces the value, i.e. buying power, of each unit of currency.

**Discuss strengths and weaknesses of the model**

- Strengths: increased competition, greater efficiency, infrastructure improvements, lower prices and increased foreign investment
- Weakness: widening wealth disparities, externalities (i.e. environmental degradation, poor labor standards), “race to the bottom.”

**Introduce concepts of efficiency and equity**

Why do we want efficiency? Why do we want equity? How do you balance these two goals? What constitutes an acceptable standard of equity (pareto-optimality, Hicks-Kaldor etc.)? Why does increased efficiency often lead to a decrease in equity? What sorts of indicators are and are not taken into account when measuring economic growth?

**Potential problems with the free market system**

- Unfair competition: monopolies can manipulate prices and wages to their advantage, often hurting consumers and/or workers.
- Under-provision of public goods: the free-market does not provide things like roads, education, public security, or justice systems because once produced these goods and services are freely available for use by everyone.
- Externalities: Producers do not internalize all of the costs of production and pass them on to society in the form of poor labor conditions or environmental pollution.
- An unchecked market results in wealth disparities.

**The role of International Financial Institutions (IFIs)**

International financial institutions like the International Monetary Fund (IMF) and the World Bank encourage developing countries to follow the neoliberal model. These institutions are lending agencies like banks. Its is important to know that because these institutions are headquartered in the United States, and because the U.S. is a major donor nation, the American government has considerable influence over IMF and World Bank policies.

These institutions encourage the adoption of neoliberal policies in the developing world by placing conditions on the loans they give out. For example, in the 1970's, Mexico began borrowing massive amounts from these institutions. Because its economy was in shambles in the early 1980's, it was having a hard time paying back these loans and as a result the IFI's imposed certain conditions on these loans. These conditions are known as Structural Adjustment Programs (SAPs).

These SAPs called on Mexico to stabilize its economy by implementing neoliberal policies like:

- Reducing the role of the state in the economy
- Cutting public spending; this would include spending cuts on education, housing, health care and transportation.
- Cutting subsidies
- Promoting the development of export industries.
- Reducing trade and investment regulations.

So what does this alphabet soup of IFTs and SAPs really mean? To look at the issues involved on a more a concrete level, we can use a family as an example. As a family you have certain expenses (i.e. doctor's bills, food, education, clothes, transportation and fun things like going to movies etc.). Let's say you don't have enough money to pay all of these expenses. So, you go to a bank for a loan. The bank gives you a loan but places SAPs on you. What does that mean? You have to make some changes to the household economy. You have to start cutting back here and there in order to get your economic house in order. In order to pay back your loans, you may have to go to fewer movies, buy fewer school supplies, go to the doctor less often, and spend less money on gas for your car. Similarly, SAP's require that governments spend less money on health care, education, transportation, and social spending in general in order to pay off their loans.