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Critically Examine the Contradictions between the Structuralist and Dependency schools: A Third World Perspective.

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Abstract:

Compare and contrast the Structuralist and Dependency schools of thought on the issues of development in the third world. Critically examine their contradictions. It will also contrast their arguments on the non-feasibility of the export-oriented strategy or the import-substituting industrialisation for the third world countries to break out of this dichotomy.

Key Words: Dependencistas, Core, Periphery, Unequal dependence, Third world

Introduction: The present paper tries to compare and contrast structuralist and dependency schools of thought on the issues of development in the third world i.e. what kind of relation is between Centre (Developed Countries) and Periphery (Third world countries) through ages and what happened to the development story of third world countries with this relation according to Structuralist and Dependency schools of thought? This paper also examines the contradictions of both structuralist and dependency school of thought. But before comparing and contrasting the structuralist and dependency schools of thought, it would be worth to know what structuralist and dependency schools of thought are, how both the schools emerged and what are their contributions to the political economy?

Structuralism: Structuralism was the first significant contribution in the field of political economy to arise from Latin America. It is primarily concerned with the exploitation of developing countries (periphery) by developed countries (centre) through trade if periphery trades those commodities in which it has a comparative advantage. Therefore, structuralists suggested that it is better to shift from primary exports to import-substituting industrialisation (ISI) with government promote industrialisation through subsidies, infrastructure, etc.

History of Structuralism: Most Latin American countries experienced import-substituting industrialisation (ISI) between the early 1930s and mid-1980s. ISI is an industrialisation strategy that focuses to deepen and integrate manufacturing industry with primary objective is to replace imports. *In most of the Latin American countries, ISI started because of the*

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success of primary product exports like coffee, sugar, rubber, tin, copper, etc. and this success in primary activities fostered the expansion of complementary sectors, especially transportation, storage, finance, trading. And as a result of the expansion of complementary sectors expansion of manufacturing sector started in locations near to centres of primary activities.

World War II leads to the breakdown of international trade and leads to powerfully accelerated ISI and several countries in Latin America turned net creditors for the first time and held large foreign currency reserves. Average GDP growth rate in these countries was 5.8% between 1945 and 1954 (Alfredo, Saad-Filho). In 1950, Raul Prebisch was appointed as executive secretary of United Nations Economic Commission for Latin America (ECLA or CEPAL in Portuguese and Spanish). He outlined in his report that there is a transition going on from primary-led growth to import-substituting industrialisation. *He also mentioned the limitations of the previous growth model i.e. exporting primary products to the centre at a cheaper rate. This report became the foundation of Latin American Structuralism.*

Principles and features of Structuralism: The Structuralists were heavily influenced by Keynesian economics and claimed that markets always do not clear itself especially in developing countries and therefore. ***The government should intervene in promoting manufacturing*** at the expense of primary activities. However, they suggested that rapid long-term growth was more important than stability and in this case they are different from Keynesian economists. Structuralists argued that there exists dualism in the periphery as there are two sectors one is the primary export sector with high productivity but large surpluses are taken away by centre through trade and rest is wasted through the import of luxury goods. The other sector is manufacturing which is relatively inefficient. While on the other hand productivity is high in almost all sectors in the developed countries (Centre). ***So, according to structuralists dualism in the world economy and periphery is due to extensive exploitative economic and social conditions.***

Structuralists in Latin America were opposed to neoclassical theory. Neoclassical theory says that a country should specialise in those commodities in which they have a comparative advantage. But Structuralists strongly argue that free trade and existing division of labour in the centre and periphery benefit centre at the expense of periphery. So, there is deterioration of terms of trade of periphery (Prebisch-Singer hypothesis). So, *it is the structure that leads to deterioration of term of trade.* The term of trade is the ratio of unit prices of exports to unit prices of imports of a country. Deterioration of terms of trade can analyse from both demand and supply side as follows:

Analysis of Prebisch-Singer hypothesis from Supply Side: There are two sets of countries Centre and periphery. Centre produces manufacturing goods while periphery produces only agricultural goods. There is a huge reserve of unemployed and underemployed workers in the agricultural sector (Periphery) so that workers can be hired without increasing wages. While unemployment is less in the manufacturing sector (Centre) and labour class is unionised. Suppose, there is an increase in productivity in the agricultural sector, unit costs

will decline, and therefore output prices fall because of competition. Centre, therefore, gets agricultural goods at lower prices. On the other hand, if there is an increase in productivity in Manufacturing sector wages will also increase, and it will lead to a rise in the price of manufactured goods. Periphery, **therefore**, gets manufactured goods at higher prices. Supply side argument can be checked numerically as follows:

$$\text{Terms of Trade} = P^a / e.p^m$$

Where P^a is Price of Agricultural good. P^m is the price of manufacturing good e is the nominal exchange rate.

The price equation can be written for agricultural sector as

$$P^a = \mu^a \cdot W^a \cdot L^a$$

If productivity rises, L^a (labour) will decrease but as there exists huge army of labour wages (w^c) will not increase despite the increase in productivity, and hence P^a will decrease, therefore periphery export agricultural goods to the centre at lower prices.

The price equation can be written for manufacturing sector as

$$P^m = \mu^m \cdot w^m \cdot L^m$$

If productivity rises, L^m (labour in the manufacturing sector) will decrease, but as there are unionised labour wages i.e. w^c (wage rate in the manufacturing sector) will also increase with the same magnitude as L^m . Therefore, Prices in manufacturing sector doesn't decrease with productivity growth. Therefore, centre exports their manufacturing products to the periphery at higher prices. Since the P^a decrease and P^m remains constant. Therefore, $P^a / e.p^m$ will decrease, i.e. deterioration of terms of trade of periphery.

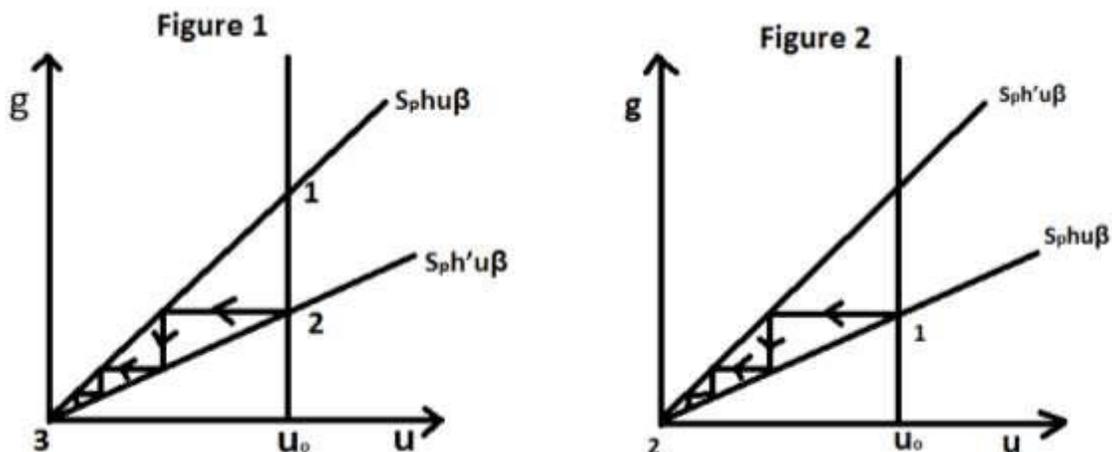
Analysis of Prebisch-Singer hypothesis from Demand Side: There are two types of goods necessities (food) and luxury (manufactures). Income elasticity of demand for necessities is less than one, and income elasticity of demand for luxury is greater than one. If periphery exports necessities and centre exports luxury, as income increases in periphery its imports to consumption ratio will increase, leading to excess demand for import (luxury) and it will lead to increase rise in the price of a luxury good and as a result terms of trade deteriorate. On the other hand, if there is a rise in income in the centre they will decrease the consumption of necessities (food) as its income elasticity of demand is less than unity. Therefore their import bill will decrease and there terms of trade improves. ***Therefore, Structuralists claim that the only way to escape from this vicious circle is Industrialisation within the economy.*** The manufacturing expansion would help to avoid deterioration of terms of trade in fact; it will improve its terms of trade. Therefore it would provide the alternative engine to growth, alleviate poverty and improves the standard of living.

Therefore, Structuralists claim that the only way to escape from this vicious circle is Industrialisation within the economy. The manufacturing expansion would help to avoid deterioration of terms of trade in fact; it will improve its terms of trade. Therefore it would provide the alternative engine to growth, alleviate poverty and improves the standard of living.

The decline of Structuralism: In 1960s ISI suffered from various external as well as internal factors. Quality was poor of manufactured exports as compared to the developed countries. Prices of manufactured goods were higher due to low productivity as well as due to overvalued exchange rates in most of the other countries. The Bolshevik revolution made all the elite class into one counter-revolutionary coalition to stave off socialism, and this made bourgeoisie align with feudal interests and become pacifists towards foreign capital. Internally, savings were very less to finance investment in the manufacturing sector because there is huge labour class in the periphery and they only get subsistence wages. However, there was also a wealthy group who mimic the lifestyle of the originating from the centre, and therefore it spends it most of the income on luxury (imported) goods. There was also the skewed distribution of land and income in periphery and tax structure was inefficient and regressive. There was a lack of infrastructure available for manufacturing growth. Therefore structuralists claimed that there was a need for state intervention to expand manufacturing sector using progressive taxation, improving infrastructure, stimulate growth, providing subsidies, protect infant industries, attract foreign investment, control over foreign exchange. In short, for structuralists, capitalist development was the possible way in developing countries through industrialisation with state intervention.

3. Dependency Theory: It is primarily concerned with the exploitation of developing countries (periphery) by developed countries (centre) through different forms of extraction of surplus and various mechanisms of transfers of surplus from periphery to the centre.

3.1. History of Dependency Theory: Dependency theory came into the picture for the first time in the 1960s and deepened its root in 1970s. It was primarily inspired by structuralism in Latin America and by 'Monopoly Capital School' of US. It is influenced by structuralism because in structuralism as we have discussed above, the world is divided between centre and periphery and surplus of the periphery is extracted by centre through trade (Prebisch-Singer Hypothesis). Dependency theory also classified that there is a division of the world in two parts centre and periphery and there is an unequal exchange between these two areas, and it leads to extraction of economic surplus from periphery to centre. Monopoly Capital theory was first developed by Baran (1957) and Sweezy (1966). According to them, there is a transition that took place in developed countries from competitive capitalism to monopoly capitalism. And today capitalism became highly concentrated and centralised i.e. it is dominated by some large corporations (Monopolies). Because of increase in monopoly power, there is an increase in prices about wage. Monopoly capitalism is stagnant in nature and slows down the pace of technical change. The decline of costs (including wages) creates the problem of absorption of surplus in developed countries which in turn creates the problem of lack of demand in these countries. This surplus can be addressed through wasteful expenditures, militarism and imperialism. The equilibrium conditions in competitive and monopoly capitalism can be understood more clearly with the help of following diagrams and their explanations.



S_p = saving rate out of profit , h = Profit/Output ,
 u = capacity utilisation [actual output (O)/potential output (O^*)]
 β = output-capital ratio, $S_p h u \beta$ = warranted rate of growth.

If there is competition in the market then adjustment between demand and supply could take place through mark-up adjustment which in turn affects the profit of capitalist to output ratio i.e. h ($h = P/O$). This adjustment can be explained as follows: In figure 1, initially actual rate of growth is equal to warranted rate of growth and therefore we are at point 1. Now suppose there is a fall in demand then actual growth will decrease, and therefore we move to point 2. Price will decrease because of lack of demand.

$$\text{Price} = \mu \cdot w$$

$$\text{or, } \mu = \text{Price}/w$$

Where μ is the mark-up i.e. claim of the capitalist in total output. W is the total wage bill of the labours. Since price has decreased, and w is constant (because of unionised labours), μ will decrease. Profits of capitalist will decrease, and therefore h will decrease, and as a result, actual growth shifts downward from $S_p h u \beta$ to $S_p h' u \beta$. Therefore the equilibrium point is 2 in the case of competitive capitalism.

But, If there is monopoly capitalism then the markup is inflexible since monopoly capitalist doesn't want to reduce his share of profit. So, the burden will fall on capacity utilisation and hence you will decrease, and this further lead to a decrease in g and this procedure will continue till reach at point 3 where g is 0, and therefore any fall in investment from its warranted level takes it all the way down to stagnation.

Figure 2 explains the transition from competitive capitalism to monopoly capitalism and then move to stagnation. Initially actual growth rate was $S_p h u \beta$ (in competitive capitalism) but over the period monopoly power has increased, and as a result, h increases and therefore actual growth become $S_p h' u \beta$. With monopolisation capacity utilisation has decreased as

shown by arrows which in turn lead to a decrease in g and this movement will continue till we reach at stagnant growth i.e. at point 2.

According to Baran (1957), because of increase in monopoly power, there is an increase in prices about wage. Monopoly capitalism is stagnant in nature and slows down the pace of technical change. The decline of costs (including wages) creates the problem of absorption of surplus in developed countries which in turn creates the problem of lack of demand in these countries. This surplus can be addressed through wasteful expenditures, militarism and imperialism. It has been seen historically that centre developed at the expense of periphery through colonialism, imperialism, looting and plundering which in turn, created under-development in the third world. Frank (1966) suggested that there exists a chain system of metropolis-satellite i.e. chain of satellites, satellites of satellites. The export sector in the periphery is a satellite of centre (Metropolis) and simultaneously export sector become a metropolis on primary sector. This chain is the cause of 'Development of Underdevelopment' of periphery through a transfer of surplus. According to Wallerstein (1974), it is the division of labour across centre and periphery that sets terms of exchange between the two. There is a dominance of centre over periphery that leads to transfer of surplus. Amin (1976) suggested that different modes of production generate dependency of the periphery on centre. Accumulation creates divergence in social formations in centre and periphery and because of this divergence labour is specialised in the centre and get high wages while there is a huge army of labours with low skills wages are low in the periphery. So, with the rise in wages in the centre and low wages in the periphery, goods were exchanged on unequal terms. This is the source of unequal exchange.

Principles and features of Dependency Theory: Dependents are opposed to the neoclassical school of thought and were not for international trade. According to them, the relation between centre and periphery, division of labour and different modes of production in the centre and periphery help to transfer of economic surplus from periphery to centre through unequal exchange, debt repayment, capital flight, etc. Dependency theory rejects dualism. Dependents suggested that there is no sharp difference between manufacturing and primary sector in periphery and backwardness in the periphery is not due to lack of capitalist development but because of the prevailing relationship between centre and periphery. Dependence of periphery on centre created a ruling class in periphery called comprador or lumpen bourgeoisie. This class exploits the locals on behalf of the centre. They export the domestically produced goods and import luxury goods from the centre. This results in a lack of investment in periphery and growth stagnated. Any capitalist development in the periphery would bring stagnation and would further deepen the underdevelopment process. The relationship of the periphery with the centre had generated a process of 'development of underdevelopment'. *In short, industrialisation was not the solution for them because the industrialists in the periphery would work for the centre and would continuously exploit working class and help in transferring the surplus to the centre. Dependents are for delinking the relation of the periphery with the centre. Therefore, periphery can develop only after social reforms. Therefore socialism is the only alternative.*

So, far we have discussed how both the schools emerged, what are their principles and features. And the above explanation is sufficient to compare and contrast the two.

Comparison and contrast between structuralists and dependency theory

4.1. Similarities between structuralists and dependency theory: *Both the schools of thought suggested that there exists a relationship between centre and periphery and this relation whether through trade, colonialism, imperialism or unequal exchange help centre in extracting economic surplus from the core. Both the schools of thought are opposed to the neoclassical school of thought.* Neoclassical theory says that a country should specialise in those commodities in which they have a comparative advantage. But according to structuralists have argued that if we trade in specialise commodities, then there would be deterioration of terms of trade of periphery (known as Prebisch-Singer hypothesis). While dependency school argued that any relationship between would result in exploitation. Emmanuel Arghiri (Dependency theorist) argued that there exists wage differential in centre and periphery and it creates an unequal exchange. Periphery (low wage country) has to pay more for its imports from the centre (high wage country). Therefore trade is not profitable, and it results in exploitation of periphery. ***Keynesianism and Marxism heavily influenced structuralists as well as Dependistas both.*** Structuralists emphasised that industrialisation should take place with government promote industrialisation. While dependency theory school emphasised that government should intervene but for political and social reforms, for equal distribution of land and income.

4.2. Differences between structuralists and dependency theory: *Structuralists claimed that there exists dualism in the world economy.* Dualism exists in the periphery because there exists two kinds of sectors i.e. one is the primary export sector with high productivity but large surpluses are taken away by centre through trade and rest is wasted through the import of luxury goods. The other sector is manufacturing which is relatively inefficient. While on the other hand productivity is high in almost all sectors in the developed countries (Centre). *While dependency school of thought rejects dualism.* Dependistas suggested that there is no sharp difference between manufacturing and primary sector in periphery and backwardness in the periphery is not due to lack of capitalist development but because of the prevailing relationship between centre and periphery. Frank wrote in his paper that the entire 'dual society' is false and rejected the dualism nature of the periphery. *Structuralists claim that the only way to escape from this vicious circle is Industrialisation within the economy with the help of government promoting industrialisation* providing subsidies, improving infrastructure, stimulate growth, protect infant industries, attract foreign investment, control over foreign exchange. According to them, manufacturing expansion would help to avoid deterioration of terms of trade in fact; it will improve its terms of trade. Therefore it would provide the alternative engine to growth, alleviate poverty and improves the standard of living. While on the other hand, *school of dependency theory argued that industrialisation is not the solution to escape from the exploitation of periphery from the core* because industrialisation needs foreign capital and if foreign capital entered in the periphery, industrialists would exploit the locals on behalf of centre, and therefore

industrialisation would not work. Any capitalist development in the periphery would bring stagnation and would further deepen the underdevelopment process. Therefore, Dependents claimed that the only solution is socialism.

5. Contradictions of Structuralism: Structuralists suggested that despite export of agricultural products focus should be on expanding the manufacturing sector i.e. establish ISI and should not export those commodities in which there is a comparative advantage. *But neoclassical school criticized structuralists* and suggested that if periphery shifts its interest towards manufacturing sector in which periphery does not have a comparative advantage, then there would be a misallocation of resources in present and growth would reduce in future. Further, if periphery import technology from centre to expand its manufacturing sector, then there would generate manufacturing inefficiency because these technologies are highly capital intensive and therefore lead to urban unemployment and also these technologies required huge market size. Therefore to operate the manufacturing industries government need to provide subsidies for a long period as these inefficiencies could not overcome within night. But this is highly expensive and wasteful. Therefore state intervention would lead to increase in inflation with increased fiscal deficit. The neoclassical theory also criticizes Prebisch-Singer hypothesis and suggested that Prebisch-Singer hypothesis is either methodologically flawed or inconclusive. Therefore for periphery, there is need to shift of investment back to primary export commodities, diversification in exports. *Kalecki (1962) in this context said that industrialisation is possible at the expense of agriculture and it will, therefore, lead to increase in the trade deficit. Structuralists claim that the only way to escape from this vicious circle is ISI with the help of government promoting industrialisation.* According to them, manufacturing expansion would help to avoid deterioration of terms of trade in fact; it will improve its terms of trade. Therefore it would provide the alternative engine to growth, alleviate poverty and improves the standard of living. While on the other hand, *school of dependency theory argued that industrialisation is not the solution to escape from the exploitation of periphery from the core* because industrialisation needs foreign capital and if foreign capital entered in the periphery, industrialists would exploit the locals on behalf of centre, and therefore industrialisation would not work. *In this context, Frank explained that why industrialisation is not the solution by taking the example of Brazil.* During World War I, World War II and Great Depression Sao Paulo became an industrial hub. But Frank claimed that this industrial development could not move out Brazil from the cycle of the metropolis-satellite system. In fact with industrial development at Sao Paulo, development has converted other internal regions into satellite, de-capitalised them further and deepened story of underdevelopment.

6. Contradictions of dependency theory: Theories of dependency school were theoretical inconsistent and therefore lead to the collapse of dependency theory. If we carefully look into the theory suggested by Paul Baran, we would get to know that there is a lack of consistent foundation. He suggested that ruling class would not give up their power on their own and if there is any threat of social reform like protests against ruling class, then policy

Critically Examine the Contradictions between the Structuralist ... Sushant Kumar Singh would move in the direction of military dictatorship. Such kind of revolts can't be avoided though it may take few years. He further suggested that class alliance has to be broken. The new ethos of collectivism would generate where the interest of society will be greater than the interest of the few. This transition may be painful because land not given to farmers may be taken forcefully. Corrupt officials would be removed by violent actions. Dependency theory claimed that all countries involved in the trade are equally capitalists and *it is the connection between centre and periphery that determines underdevelopment of periphery. But if it is the case then why dependency theory failed to explain the success stories of 'East Asian Tigers', Canada, Ireland and Japan. These all became developed despite their connections with developed countries.* Frank (1966) focused on the transfer of surplus from periphery to the core and suggested that delinking is the only solution to the problem of underdevelopment. But according to Patnaik (1997), it is the structural constraints that are arising from the interaction between centre and periphery and restrict the pace of development of periphery. *Further, Patnaik criticises Frank and suggested that the facts that attempts of delinking are fraught with contradictions. Therefore delinking is not the solution. The real question is that how to delink?* The theory of monopoly capital and dependency theory did not define monopoly power clearly and could not explain how it arose. Monopoly capital theory underestimates the role of demand in the determination of prices and focuses on the market size. The concept of 'surplus' developed by Baran and Sweezy (1966) were also questioned. *The concept of unequal exchange developed by dependency school was criticized by Patnaik and suggested that any concept of unequal exchange has to have a benchmark of 'equal exchange' and it is not that easy to define such a benchmark or norm. If rate of profits are equal in core and periphery but only differences in wages exists then this it lead to unequal exchange (Wallerstein 1974). But the point to note that it is not the advanced countries that exploit third world countries but there is exploitation itself within third world. Therefore the theory of unequal exchange is not consistent. Further, even if we accepted this theory it would still fail to provide an explanation of uneven development. Finally, it has been found empirically and historically that calculations on 'transfer of surplus' through unequal exchange are coming out to be so small. Therefore theory of unequal exchange underestimates the impact of imperialism in context of third world.*

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