Dualistic Theories:

- There are different theories which are of the view that the poverty and underdevelopment of poor countries is attributed to their dualistic character.

  (1) Social Dualism,

  (2) Technological Dualism and

  (3) Financial Dualism.

(1) Social Dualism or Sociological Dualism:

- **Definition and Explanation:**

- **J.H. Boeke** is a Dutch Economist who studied Indonesian Economy and presented his ***theory of social dualism.*** He maintains that there are three characteristics of a society in the economic sense. They are as:

(i) Social Spirit
(ii) Organizational Form
(iii) Techniques Dominating Them.

Their inter-relationship and interdependence is called the ***social system or social style.*** A society is homogeneous if there is only one social system in the society. But the society which has two or more social systems is known as ***dual or plural society.***

- Dr. Boeke says that the *dual society* is a society which has *two full grown social styles* which represent pre-capitalism and post-capitalism. Such a dual society is *furnished with the existence of an advanced imported western system on the one side and endogenous pre capitalistic agricultural system* on the other side.
- The former is under the western influence which uses the advance techniques and where standard of living is high.
- The later is native and it is furnished with the outdated techniques and low social and economic life. This is **called social or sociological dualism** and *these two systems are clashing*. The imported social system is highly capitalistic and it may be socialistic as well as communistic system.

• Characteristics of Dualistic Society:

On economic basis the dualistic society is classified as by giving the names:

(i) Eastern Sector and

(ii) Western Sector.

There are certain ***characteristics of eastern sector of a dualistic economy*** which distinguishes it from western sector. They are as:

(i) The needs of eastern sector are limited. People pass a contented life.

(ii) People work for social needs rather for economic needs. For example, if a three acres are enough to supply the needs of a household he will not cultivate six acres.

(iii) Goods are cultivated according to their prestige value rather on their use value.

(iv) As a result of all above, the eastern economies are characterized with backward bending supply curves of effort and the risk taking.

(v) The native industries have neither organization nor capital and they are ignorant of modern technology and market conditions.

(vi)People are indulged in speculative activities rather in business enterprises.

(vii)They do not take risk by making productive investment.

(viii)They lack the initiative and organizational skill which is a feature of western sector of dual economy.

(ix)Labor is unorganized, passive and unskilled. They are reluctant to leave their village and community. They are fatalist.

(x)The urban development takes place at the cost of rural life.

(xi)Exportation is the main objective of foreign trade in the eastern sector while the western sector believes in imports.

Due to these features of eastern society the western economic theory is not applicable as far as LDCs arc concerned.

- The ***western economic theory*** is meant to explain capitalistic society whereas eastern sector is pre capitalistic. The western sector or society is based upon *unlimited wants* and *money economy* etc. Moreover. The MP theory cannot be applied in LDCs for resource allocation and distribution of income because of immobility of resources. Thus **Boeke** says:

- We should ***not*** try to transplant the delicate houseplant of western theory to tropical soils where an early death awaits for it. If the pre-capitalistic agricultural sector of eastern sector is attempted to develop along western lines it will *create retrogression*.
- The modern agricultural techniques can not be applied how-long the mental attitudes of the farmers are not changed, otherwise *the increase in wealth following modern technology will result in further growth of population.*
- *Moreover, in case of failure of modern technology, the indebtedness of the country will increase*. *Therefore it is better that these existing agricultural systems should not be disturbed*.

- As far as industrial field is concerned the eastern producers cannot follow the western technology on the basis of economic and social reasons.
- He says that *the adoption of western technology to industrialize Indonesian economy has moved the goal of self sufficiency farther and ruined its small industry*.

- **Boeke** refers to ***five kinds of unemployment in UDCs:***
  (i) Seasonal, (ii) Casual, (iii) Unemployment of regular workers, (iv) Unemployment of white collard class, (v) Unemployment of Eurasians.

- According to Boeke the *govt., is unable to remove such unemployment* because of the reason that it will require the funds which the govt. cannot avail.
- Boeke says that *limited wants and limited purchasing power in eastern sector hamper economic development*. If the food supply is increased or industrial goods are increased, it will bring a glut of commodities in the market. The prices will fall and economy will face depression.
- But this does not mean that Boeke is against industrialization, and agricultural improvement. Rather *he is in favor of slow process of industrialization and agricultural development on small scale which could have an adaptability with the dualistic structure of eastern society*.
- *The urge for development should come from the people themselves*. New leaders must emerge who should work for the goal of development with faith, charity and patience.

Criticism:

- **Professor Bengmin Higgins** has criticized the social dualistic theory on the following grounds:

(i) Wants are not Limited: If we analyze "Indonesia's life" we do not find that the desires of the people are limited. This is the reason that the govt. has to impose import restrictions. Moreover, whenever the harvest is good the farmers become prosperous and the demand for luxurious goods rises.

(ii) Casual Labor are not Unorganized: Boeke presented the version that casual workers are unorganized and passive. But this may be true as far as agricultural sector is concerned but they are not unorganized in coffee, tea, rubber and plantation etc.

(iii) Eastern Labor is not Immobile: Boeke thought that eastern labor is immobile. It is not so because of attraction of modern facilities of life in the urban areas. Moreover the high income incentives force the labor to move from rural areas to urban areas.

(iv) Dualistic Theory is not Particular To UDCs Only: The eastern society, according to Boeke, only exists in UDCs. It is not true. It does exist in Canada, Italy and even in the United States.

(v) Applicability to Western Society: According to Professor Higgins most of the characteristics of eastern society given by Boeke are present even in the western societies. For example, during hyper inflation, speculation is preferred to investment. This means, the people in the western countries also have a strong desire to keep their capital safe and in liquid form, The western society also believes in conspicuous consumption as discussed by Veblin and Snob effects. The backward bending supply curve of efforts has been experienced by Australia during post war period and by US in the fifties.

(vi) Not a Theory But a Description: It is objected that the Boeke's dualistic theory is merely a description rather than a theory. His findings are based upon neo-classical theory which has the limited applicability in the western world.

(vii) Does not Provide Solution to the Problem of Unemployment: Boeke's dualism centers more on socio-cultural aspects rather on economic. He only says that govt. is not in a position to remove unemployment. Moreover, he does not mention the situation of under employment. Therefore his theory is full of shortcomings.

Conclusion:

- The main problem of dualistic economies is to provide employment opportunities and Boeke theory fails to do it. Therefore, Prof. Higgins has developed the theory of technological dualism.

(2) Technological Dualism:

- **Definition and Explanation:**

- ***Professor Higgins has developed the theory of Technological Dualism.*** By this we mean:

"The use of different production functions in the advance sector and in the traditional sectors of UDCs".

The existence of such dualism has increased the problem of structural or technological unemployment in the industrial sector and disguised unemployment in the rural sector. Higgins theory of technological dualism incorporates the factor proportion problem as discussed by **K.S. Eckaus,** which is related to limited productive employment opportunities found in the two sectors of a UDCs because of market imperfections, different factor endowments and different production functions.

The UDCs are characterized with structural disequilibrium at the factor level. This arises, because a single factor gets different returns in different uses or *because price relationship among factors are out of line with factor availabilities. Such disequilibrium leads to unemployment or underemployment in two ways. It is as:*

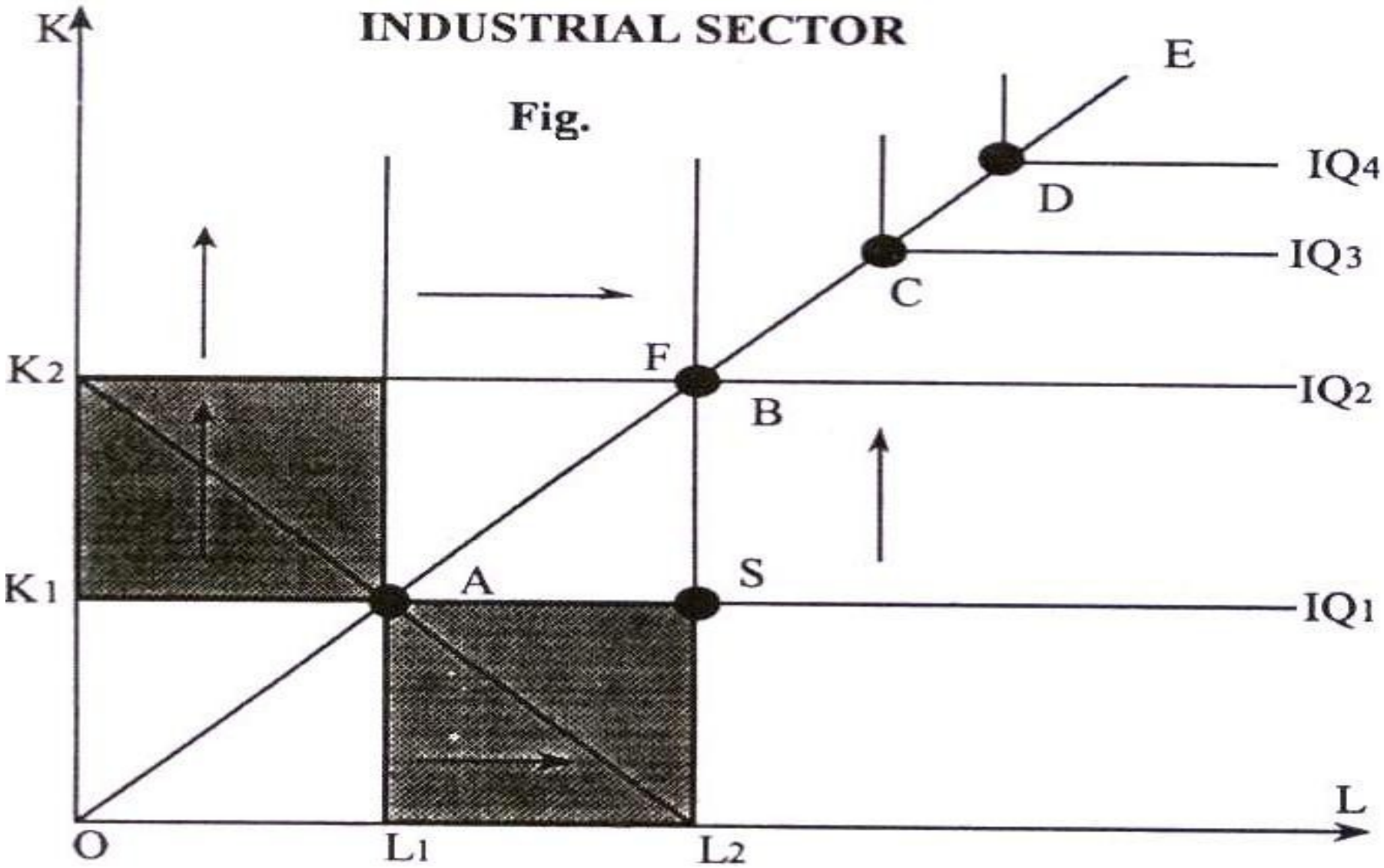
(i) Imperfection of price system.

(ii) Structure of demand which results in surplus labor in overpopulated backward country.

- *Thus the technological unemployment in UDCs is because of surplus labor which results from misallocation of resources and structure of demand.*

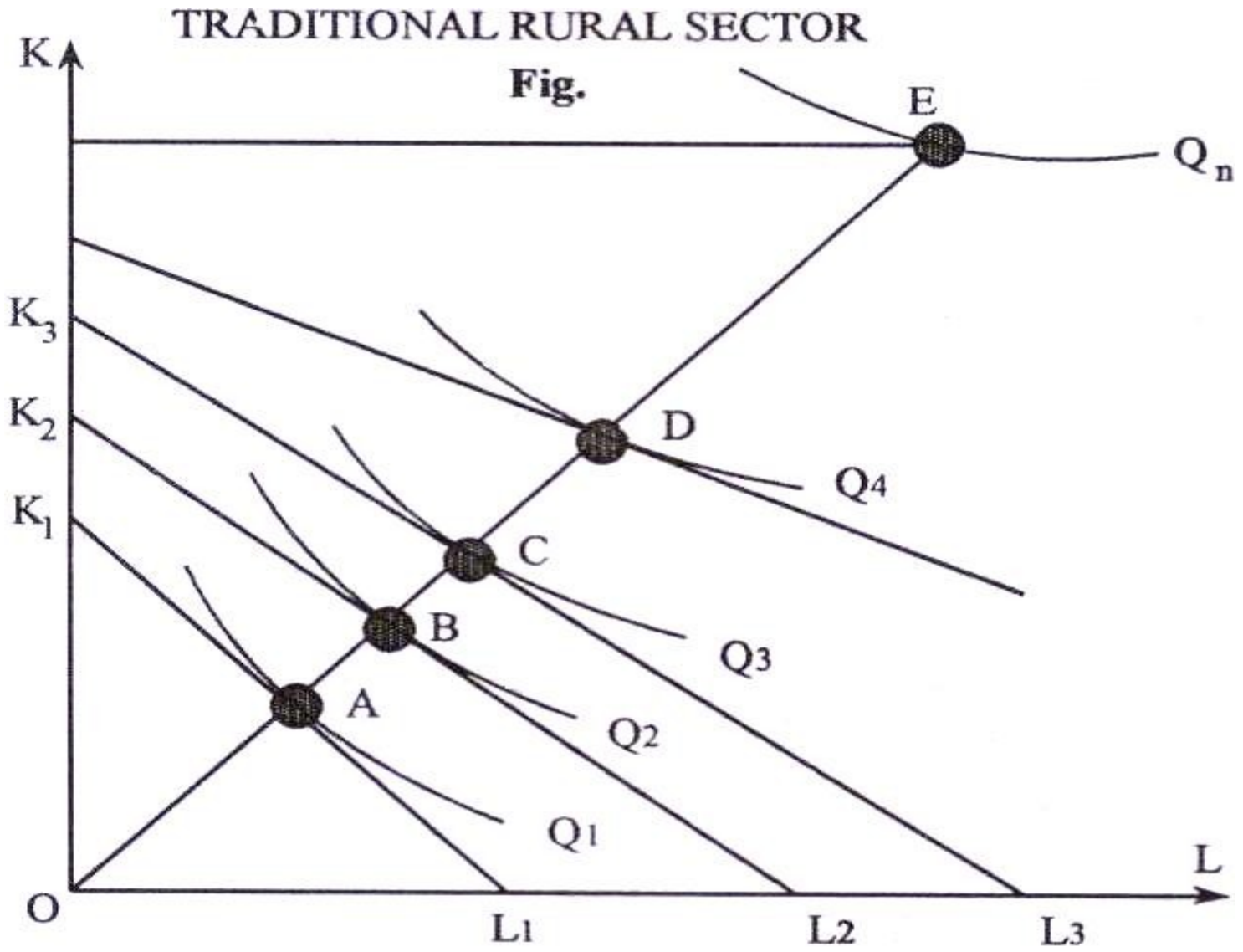
- Higgins constructed his theory by assuming ***two goods***; ***two factors*** and ***two sectors*** and their factor endowments and production functions.
- Of these two sectors the **industrial sector** is engaged in plantation, mines, oil field and large scale industry. It is *capital intensive* and characterized by *fixed technical coefficients* that is, the factors have to be combined in a fixed proportions.
- While the **rural sector** is engaged in producing food stuffs, handicrafts and very small industries. It has changeable technical coefficients of production. Hence it has different alternative combinations of labor and capital. The production functions in the industrial sector are represented as in figure:

Figure/Diagram:



- Here the IQ_1, represents the combination of OL_1, of labor (L) and OK_1, of capital (K) which produces a certain level of output. While IQ_2, IQ_3 and IQ_4 represent higher level of output which arc only possible if K and L are increased in the same proportion. Thus the points; A, B, C and D show fixed combinations of capital and labor which are used to produce different levels of output.
- The line OE represents ***expansion path*** in the industrial sector and its slope represents constant factor proportions. The line K_2L_2 shows that the production process is *capital intensive*. To produce Q_1, output OK_1 of K and OL_1 of L are used. If the actual factor endowment is at S rather A. It means that more labor are available to produce same amount of output. While here units of K are OK_1.
- *Since there are fixed technical coefficients, the excess labor supply will not affect the production techniques at all. The L_1L_2 units of labor will remain unemployed*.
- *It is only when capital stock increases to SF, then it will be possible to absorb this excess labor supply in this sector. Otherwise it has to seek employment in rural sector.*

- The production functions for rural sector are shown in the figure:



- The isoquants, Q_1, Q_2, Q_3 and Q_4 show variable coefficients of production. In order to produce more output more labor is employed as compared with the capital. As a result the good land (capital) becomes scarce and all available land is cultivated by *high labor intensive techniques*. At point E where maximum output level is reached as shown by Q_n.
- Thus, according to Higgins, because of different production functions the *unemployment* and *underemployment* comes into being in UDCs.
- *According to Higgins the industrial sector uses capital intensive techniques and fixed technical coefficients and it is not in a position to create employment opportunities at the same rate at which population grows. Rather, the industrialization reduces the employment in this sector. Therefore, the rural sector is an alternative for the surplus labor.*

- *In the beginning it is possible to absorb the additional labor by bringing more lands under cultivation. This leads to optimal combination of labor and capital*.
- *Eventually good lands become scarce*. The ratio of labor to capital in that sector rises and the techniques become increasingly variable in this sector. *Ultimately all available lands is cultivated by high labor intensive techniques and MP of labor becomes zero and negative.*
- *Thus with the growth of population disguised unemployment begins to appear*. Under these circumstances farmers have no incentives either to *invest more capital* or to introduce *labor saving techniques*.
- As a result the techniques of production, the productivity of labor and socio-economic life is remained at low level in the rural sector.

- *In the long run the technological progress does not help in removing the disguised unemployment. Rather it tends to increase the number of disguised unemployed.* ***The situation is further aggravated by keeping wage rates artificially high by trade unions or by govt. policies****.*
- *For high industrial wages relative to the productivity provide an incentive to the producers for introducing labor saving techniques and thereby it diminishes the further capacity of the industrial sector to absorb surplus labor.*
- *Accordingly these factors increase the technological dualism in UDCs.*

• Criticism:

- Professor Higgins has attempted to present how disguised unemployment gradually rises in the rural sector of dualistic society. But the theory has the following defects:

(i) Assumption of Fixed Technical Coefficient: Higgins wrongly assumes fixed technical coefficient in the industrial sector without any empirical verification.

(ii) Factor Prices do not Entirely Depend Upon Factor Endowment: This theory indicates how the factor endowment and different production functions result in disguised unemployment. So disguised unemployment is connected with the factor prices. But it has been found out that the factor endowments do not entirely determine the factor prices.

(iii) Ignoring The Institutional Factors: There are many institutional and psychological factors which have been ignored by Higgins in connection with their effect on factor proportion.

(iv) Ignoring the Use of Labor Absorbing Techniques: According to Higgins that industrial sector employs highly capital intensive techniques which are imported. But practically we find that all imported techniques are not labor saving. For example, Japan's agricultural development is not due to capital intensive techniques.

(v) Size and Nature of Disguised Unemployment is not Assessed: Higgins does not clarify the nature of disguised unemployment in the rural sector and excess labor supply in the industrial sector. Moreover, he does not tell about the extent of disguised unemployed due to technological dualism.

(3) Financial Dualism:

- **Definition and Explanation:**
- **Professor Hala Myint** has developed the ***theory of financial dualism.*** Such dualism rises because of division of money markets in ***unorganized*** and ***organized*** money markets in LDCs. The *rate of interest* in unorganized market is higher than the rate of interest in organized money market which is concerned with modern sector. The unorganized money market consists of village money lenders, landlords. They charge the high interest because of the following reasons.

(i) The lenders have monopoly and position of the borrowers is very weak

(ii) There is a shortage of savings in the traditional sector because most of the savings are made in terms of land or gold.

(iii) Due to natural calamities etc. the risk attached with such lending are very high.

- Thus we find that the high interest rate which the farmers have to pay not only consists of formal interest charges but also the concealed charges obtained through under pricing the grains purchased by the farmers.

- On the other hand, in the organized markets of LDCs the interest rates are low and credit facilities are abundant. The loans are advanced to manufactured sector, export industry and modern commerce sector.

- Professor Myint says that there was an old financial dualism which used to exist in the open economy of colonial period and the financial dualism which now exists.
- Under colonial system there was perfect convertibility at fixed exchange rate. Consequently there was no shortage of foreign exchange and there were no BOP problems*. But now a days the LDC's have to face internal as well as external balance. Thus the poor traders and small peasants not only have to face high interest rates, but also the shortage of foreign exchange. Then they are not in a position to get advanced machinery etc.*

- Under colonial system organized money market of LDCs is consisted of the branches of western commercial banks which were linked with international financial market. In colonial system the modern sector consisting of mines, plantation and foreign trade borrowed at low interest rates both from western banks and the world capital markets. *But the present LDCs have attained monetary independence by establishing their own central banks. They have introduced the exchange control.*

- As a result, *the organized money market of the LDCs have been separated from the world capital market*. *Hence, their central banks are following the cheap monetary policy even when they are having shortage of funds*. They are maintaining over-valued exchange rate on the ground that devaluation will create inflation.
- On the other hand there is *chronic excess demand for foreign exchange in these poor countries*. *To meet this situation, these countries depend upon exchange controls, direct controls, monetary and fiscal policies*. **This has led to enhance the economic dualism between the traditional sector and modern industrial sector.** *The cheap monetary policy by maintaining artificial low interest rates has become helpful for the large industrial sector. The low interest rates have discouraged the flow of funds from abroad and savings from within the country. But it has created an excess demand for loans*.
- Thus the major part of domestic savings *are flowing towards industrial sector*. This has *reduced the capital to traditional and agriculture sector* which have to get at higher interest rate.

- *The foreign exchange control to correct deficit in BOP has also benefited the modern industrial sector against the traditional sector*. It is because that the major share of available foreign exchange is allocated to the industrial sector to import capital intensive goods. On the other hand, the agricultural and small scale sector fail to get foreign exchange and import permits because of red-tapism and corruption in the LDCs.
- The most of the UDC's have established agricultural banks and cooperative societies. But these institutions have been found providing loans to the influential people and to the model villages.
- All this has led to *misallocation of resources* between the modern and traditional sector. *So money markets in the LDCs remain backward*. *Domestic inflation along with over-valued exchange rate have encouraged flight of capital*. The countries where this is checked, the capital moved in the purchase of gold, jewellery, real estates and other speculative activities. This is because of low rate of interest against investment. Hence the money market remains ineffective.

- Govt. controls over the scarce supply of capital have *also retarded the growth of financial intermediaries in the LDCs*. These controls favor the large manufacturing units and the banks. They discriminate against the small borrowers and the money lenders who provide credit to the small borrowers.
- In the LDCs govts. believe that capital funds invested in durable capital goods are productive while those invested in financing agriculture and trading activities are unproductive.

- According to Myint the cheap and easy credit to the traditional sector is not provided because of following:

(i) The high over head costs and salaries of officials of commercial banks in the rural areas.

(ii) The red-tapism in dealing with small borrowers according to the rigid rules.

(iii) The lack of coordination between the head office and the branches.

(iv) Lack of subsidized loans supplied by the agricultural banks etc.

- Professor Myint suggest ***two types of policies to reduce financial dualism in LDCs:***

(i) The official interest rate in the organized capital market be increased. This will attract the savings both from the country and out of the country. It will also create an equilibrium between the demand for loan able funds and supply of loan able funds.

(ii) There should be free access on equal terms to capital funds by modern and traditional sector. This will reduce misallocation of resources between the two sectors.