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# Is there an endogenous relationship between culture and economic development?

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## Abstract

Evidence from two communities suggests diverging paths of economic development; one which integrates culture into economic activities, and a second path which does not. If endogeneity cannot be assumed, does the relevance of culture for economic activities influence its stability and sustainability? Despite the predominance of culture in the former community, the social norms, ethnic cues and symbols are neither more likely to thrive or survive. Against expectations, the latter group appears more successful in preserving culture through a strategy of separating social identity from economic activities. © 2002 Elsevier Science B.V. All rights reserved.

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## 1. Introduction

It is widely accepted that the institutions and laws of a country affect economic opportunities and constraints. With the explosion of countries making the transition to democratic capitalism, political scientists and economists renewed the study of institutions and laws which promote democracy at the same time as they maximize economic efficiency and growth. As behavior does not conform to expectations, explanations frequently turn to the endogenous relationship between culture and economic development. While including culture in development is the right direction there is cause for careful consideration of the way it is included in analyses. It used to be that culture was treated as a residual category simply filling in what could not be explained by other variables. Today, we risk placing culture as an

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omnipresent set of factors. This new wave of attention to culture carries the risk of pushing the pendulum of error from the absence or “black box” of culture to its ubiquity, and suffers to the extent that it assumes the relevance of culture for economic interaction and development.

To avoid treating culture as a residual explanation and assuming culture as relevant to all explanations, greater attention needs to be given to the specification of mechanisms by which culture interacts with political and economic development. Endogeneity is an empirical question rather than theoretical certainty and understanding the patterns, or mechanisms, which connect culture to economic factors is crucial for the study of development. At the same time, if it is the mechanisms which vary, rather than the cultures themselves, it may be possible to generalize beyond any one ethnicity. This paper focuses on the endogeneity between culture and economic development, but the emphasis on mechanisms applies similarly to studies of the endogeneity between culture and political development.

The study of the interaction between culture and economic development is not new. From Adam Smith, social science and legal scholars continue to debate economic efficiency across cultural groups as defined in recent work by Pagden (1988) and Fukuyama (1995), the relevance of uniform legal regulations to solve “market failure” in different cultural communities as explored in Chong (1996) and Sunstein (1996), and the apparent convergence of decision making processes and patterns within particular groups, for example, in Landa (1994) and Wright (1995).

Research on the endogeneity of culture and economic development include studies of culture’s effects on economic development, and studies investigating the cultural consequences of economic development. In the first area, a dominant approach explores particular cultural traits and relationships between members which promote economic activities and success in competitive environments. Early beginnings with sociologist Max Weber (1930) evolved, and more recently political scientists Bates et al. (1998) and economist Grief (1994) specify those particular sets of norms and social patterns which foster economic development. Most recently, the collected volume edited by Lawrence Harrison and Samuel Huntington, *Culture Matters* revisited cultural prerequisites of progress and concluded that certain values were more conducive to development.

Cultural norms, for example, like trust are types of symbolic credit which enhance the ability of individuals to cooperate and to forgo short run gains in transactions. When individuals are closely connected they can avoid costly contracts, avoid enforcement and measurement costs, and tap into extensive information networks. When competing against businesses compelled to incur such costs, the social cohesiveness or social capital (Putnam, 1993) brings a competitive edge that translates into higher profits and long run success. In this area of research, authors emphasize the cultural criteria for development. Bonds between individuals sharing a culture can create economic advantage. The literature on the relationship between culture and development is replete with studies focusing on the impact of cultural characteristics on political, social and economic development.

A second focus of literature explores the relationship from the perspective of the impact of development on culture. The wide range of approaches include Knight’s (1992, 1995) examination of institutions and the distribution of resources where asymmetries in power translate into the dominance of particular cultural norms. And through surveys and comparative cases, Inglehart’s research (1990, 1998) explores the causal influence of culture, but also the impact of industrialization and post-industrialization on values. Generally, studies

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