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International trade and cultural diversity with preference selection

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Abstract

We consider the evolution of preferences when trade occurs between two countries. We show that if one country is much larger than the other, the preferences of the large country can take over the preferences of the small country. This may explain why some small countries exclude certain goods (especially those related to culture) from trade liberalization agreements. We also show that when the sensitivity of preferences to relative price is high, the distribution of preferences can fluctuate over time.

JEL classification: D80; D83
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1. Introduction

There are many reasons why a country may wish to protect an industry from foreign competition. The arguments that have been put forward in favor of protectionist barriers (such as tariff or quota) include, among others, the infant-industry argument, the national defense argument, and the cultural identity argument.

Concerns have been expressed in many circles on possible detrimental effects of globalization on cultural diversity. In some countries, policy makers have taken these

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concerns very seriously. Canada and France are two G7 countries that have in place policies to prevent the possible loss of cultural identity that might result from free trade. France has restrictions on foreign films and television programs from English-speaking countries, while Canada requires minimum level of Canadian content in radio and television broadcast. Canadian magazines are protected by government tax laws that discriminate against Canadian companies that place their advertisements in foreign magazines imported into Canada (in particular, US-based magazines such as Sports Illustrated, Time, etc.). Similarly, South Korea has restrictions on music CD's imported from Japan.

There are, however, very few formal models of effects of trade on culture, or on welfare that include cultural identity as an argument. Three recent papers stand out. Janeba (2004) formalizes the notion of cultural identity and incorporates it in a Ricardian model of trade. He adopts the "identity function" formulation of Akerlof and Kranton (2000), whereby (i) a person suffers a utility loss if some individuals in his country deviate from the social norms, and (ii) an individual who deviates from social norms incurs a direct utility loss for the self-inflicted loss of identity (but he may still achieve a net gain in doing so, when the foreign good becomes sufficiently cheap). One of Janeba's results is that trade is not always Pereto superior to autarky. This is because of the public good aspect implied by (i) above. Suranovic and Winthrop (2003) present two models of trade when consumers or workers care about culture. In their first model, called the "cultural affinity from work" model, workers in a particular industry receive non-pecuniary cultural benefits (NPCB) from work. If trade liberalization causes this industry to decline, the gains from trade in the case where NPCB exist are smaller than under the standard textbook case. In their second model, called the "cultural externality model," consumption of the home-produced culture good by each person in the home country has a positive external effect on all his compatriots. As a result, the optimal tariff is positive even if the country is a small open economy (even though the tariff is inferior to a consumption subsidy). Francois and van Ypersele (2002) consider the protection of a cultural good the production of which involves a fixed cost. A tariff on Hollywood movies can be Pareto superior to free trade if it makes local movies viable.

While arguments for protection must clearly be based on the public goods or externalities associated with the production and/or consumption of cultural goods, in this paper we propose to focus on a different aspect of the problem of trade and culture: the effects of trade on the *evolution* of preferences. We provide a dynamic model which shows that, in the long run, free trade may result in the demise of cultural diversity: a relatively small country may gradually lose its cultural identity when it engages in free trade with a larger country that has a different preference pattern. Relative world price is endogenous in this model, and changes over time as the distribution of preferences evolves in each economy.

Our approach is essentially based on biological evolutionary theory, but the model must be interpreted in a broader sense, as will become clear in what follows. The argument that preferences evolve is basically drawn from the Darwinian theory of evolution[1] and can

[1] Evolution-based explanations of the prevalence of certain preference traits in human societies have been provided by Cavalli-Sforza and Feldman (1973), Hirschleifer (1977, 1978), Bergstrom (1995), Robson (1996), and others.