Business Analyst, ISSN 0973 - 211X, 40(1), 115-122, ©SRCC

CULTURE AND ECONOMIC GROWTH: A SURVEY OF THE LITERATURE

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ABSTRACT

Economists for long have been fixated with the concept of a self-interested rational economic agent. Decision making by them however is not done in isolation from the society and societal culture plays a key role there. This article provides with a review of the existing work that relates culture to macroeconomic issues like growth and development.

Key words: Culture, Development, Literature Survey

INTRODUCTION

The idea of Homo Economicus has been central to economics as a discipline. The notion of an individual decision maker who operates on his own and makes choices as a self interested entity in a rational manner has been at the crux of neoclassical economics. As Sen (1977) had rightly pointed out that "The rational economic man is close to being a social moron". The scope of economics was therefore restricted to ideas and processes that would not touch upon the social aspect of the choice problems of an economic agent.

Humans or for that matter economic agents do not operate in a vacuum consisting of only markets. They interact with people around them who comprise together to make a society. Incorporating the society related factors as key institutions in the economic sphere is not a very novel one. The idea that the societal forces interact with the economic ones dates back to Weber (1930), who in his seminal work argued that societal parameters such as religion, race and ethnicity have an effect on the economic domain.

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One of his noted arguments was that the Protestant work ethic was one of the key drivers of the development of a capitalist economic system in some parts of

Western Europe. Polanyi (1944) followed Weber's line of thought and argued about how not just an economic system is embedded in a social one but also social relations are embedded in an economic system. To quote Polanyi:

> *The term `embedded- ness' expresses the idea that the economy is not autonomous, as it must be in economic theory, but subordinated to politics, religion and social relations.*

It is since then the idea of social interactions having an interconnection with the economic realm was introduced in the discourse on economic thought laying down a foundation for the disciple to interact closely with other social sciences such as sociology.

WHAT IS CULTURE?

Social interactions therefore are expected to play a critical role in economic analysis. An important component of social interactions is what is called as `Culture'. Literature from Sociology and Anthropology has defined the term culture in multiple ways. Culture is usually defined as a sum total of values, norms and beliefs that shape up the way a society functions both through the material perspective such as implicit norms while using public transport, gestures while communicating or food habits and also in certain non tangible ways like expectations about personal space, subjective teaching methods and educational standards. This intangible or non-material part of culture is what often interrelates with the economy. A range of economic issues such as savings behavior, social capital variables such as trust, female labor force participation and fertility decisions, preferences for redistribution are the ones that relate to the cultural practices in a society and have direct consequences for the development of an economy. The next few sections provide a detailed review of the existing literature on a variety of cultural traits and their interaction with the economy and it's implication for the process of economic development.

LITERATURE ON CULTURE AND ECONOMIC GROWTH

The idea of culture and its relation with the economy was pioneered by Weber but it was only until recently that there has been a renewed interest of economists in the cultural explanations for differences in the growth trajectories of various economies. Greif (1994) revived the importance of culture in economic analysis. In this work, he analyses the relationship between cultural beliefs and the organization of two trading societies, the Maghribi's and the Genoese's. In a principal agent set up, they look at a problem wherein traders are principals who assign the job of sending their goods elsewhere through the agents. The agents potentially can steal away a part of the goods in the process, incurring loses for the principal. The Maghribi's thrived on informal institutions like trust on the agents whereas the Genoese's relied upon the formal enforcement procedures such as legal contracts. The Maghribi's therefore characterized a collectivist society and the Genoese's being an individualistic one. In this game theoretic framework he shows that the collectivist ones transform in the long run to a society with mostly horizontal relations and one with no legal formal institutional structure whereas the individualist ones have vertical structure with a formal developed legal enforcement system.

Until more recently, Guiso, Sapienza, and Zingales (2006) explore this bidirectional linkage between culture and economic development. They argue that there are two parts to culture. One is the part that is inherited and the other is what they call as `voluntarily accumulated'. They argue that they focus on the former, as that is what constitutes culture. They further argue that inherited parts of culture such as religion, ethnicity, race etc. don't evolve in a short span of time. It takes centuries for them to respond to economic conditions. Hence they use these time invariant variables for the purpose of identification of culture. Using data from General Social Surveys and World Values Surveys, they consider the linkage between culture as identified by the above variables and variables such as trust, probability of becoming an entrepreneur and few economic outcomes related variables such as savings propensity and preferences for redistribution.

Di Tella and MacCulloch (2014) using data from World Values Surveys and European Values Surveys, look at the certain beliefs about economic variables such as meritocracy and poverty to show a causal link between these and economic performance. They show that more leftist beliefs are associated with lower economic performance. They further also analyze some non-economic beliefs in the same framework and find little evidence for its relation to economic performance.

Tabellini (2010) studies the causal effect of culture on development using the data from World Values Survey opinion polls from 1990s for the European Region. They take the instrumental variable approach to resolve the endogeniety issue. They look at specific variables as outcomes considering variables on trust, confidence on the link between effort and success and also variable related to respect for others. They use historical variables on regional literacy and political institutions as instruments for culture and shows that historical variables are important factors in determining the regional level economic development.

Culture broadly affects the economy through multiple channels which have been discussed the next few sections.

I. Culture and Savings Behavior

Savings behavior of individuals varies across countries and is considered as of the key drivers of economic growth. The typical reasons that have been cited for this are related to differences in demography, tax and social security systems, macroeconomic differences like differences in income levels and growth rates and also differences in the structure of financial markets. However, apart from these macroeconomic and institutional distinctions, cultural differences have also played a significant role there. Carroll, Rhee, and Rhee (1994) study the relationship between culture and savings. They use the differences in savings pattern of immigrants in Canada with differences in country of origin helping to identify culture. Using data from Canadian Survey of Family Expenditures, they see the relation of cultural origins with the gross national savings rate from 1970 to 1985. They find no evidence for effect of culture on savings. In a similar manner Fuchs-Schundeln, Masella, and Paule-Paludkiewicz (2017) use the data from World Values Surveys, European Values Survey, Hofstede data set and Schwartz Value Survey to examine the effect on culture and savings for Germany and the UK. They find that culture plays a significant role in determining household savings behavior mostly through the channels of attitude towards thrift and importance assigned to accumulation of wealth coming from the place of origin.

ii. Culture, Trust and Risk

In addition to savings, social capital has long been recognized as a major factor contributing to economic growth and trust is one of the key elements of that. (Putnam, Leonardi, & Nanetti, 1994) Certain local economies thrive on the close-knit community structure coexisting with and also at times replacing formal and legal institutional structures. Trust in these communities however builds or gets destroyed over time. Guiso, Sapienza, and Zingales (2008) analyze inter generational transfer of beliefs on trustworthiness of others in an overlapping generations framework. Using a dynamic trust game, they show a possibility of an economy being stuck in a low trust trap. They further test their findings empirically by using World Values Survey and German Socio Economic Panel data and show persistence in trust at the low levels. Tabellini (2008) also uses an overlapping generations framework to analyze inter generational transmission of good traits that foster cooperation as an equilibrium outcome. They prove that under certain initial conditions, an economy can end up in a state of low cooperation and weak legal enforcement.

Dohmen, Falk, Huffman, and Sunde (2011) empirically test three channels through which inter generational values can be transmitted. They focus on two specific attitudinal variables, one being trust and the other being risk preference. They consider three contestable channels viz parent to the child transfer, peer effect through the local environment and positive assortative matching of the parents. Using data from the German SOEP data set, they find evidence in support of all the three mechanisms. Klasing (2014) considers inter generational transfer of risk preference in an endogenous growth model with an innovation based R& D sector that has an element of risk attached to its activity. They show that societies with preferences for risk taking ability being on the higher side, which provide greater return from the risky activity, are associated with a higher growth rate.

iii. Entrepreneurial Culture

Risk taking ability has often been connected to entrepreneurial tendencies and therefore innovation, which further is considered to be conducive for growth. Based on historical data, Mokyr (2010) argues that at the time of industrial revolution in Britain, cultural reasons were one of the crucial incentives driving entrepreneurial innovation: `Many of the industrialists in Britain were gentlemen amongst the cutting edge of science and technology to demonstrate that it was no longer frowned upon to be excited by innovation.' Doepke and Zilibotti (2008) consider this relationship between entrepreneurship, culture and growth in a model of endogenous technical change where technological development depends on entrepreneurial activity. Entrepreneurial culture, defined in terms of risk tolerance and patience, is transmitted inter generationally using a transmission mechanism to maximize child's utility. They show the possibility of multiple balanced growth paths. Chakraborty, Thompson, and Yehoue (2016) examine similar relationship in a model with human capital. Inter generational transmission of human capital depends upon the parental occupational choice. Occupational choice of an agent in turn depends on the values and perceptions about returns associated with various occupations, which are culturally transmitted.

Their model exhibits the possibility of resistance to adoption of technology by entrepreneurs, resulting in persistence of low productivity and stagnation. They further analyze the long run impact of productivity shocks and human capital shocks on such a stagnant society.

CONCLUSIONS

In the last few decades, there has been a new wave of research in the field of economics. Economists have been going beyond the idea of a rational economic agent and trying to incorporate ideas from allied social sciences to understand the decision-making processes of economic agents. Culture is one such element associated with sociology that influences the choices of an economic agent and at the same time is shaped up by these individual choices. The dependence of these two fields on each other has now become a key element of research in economics. Both theoretical and empirical work is being done at this interface of the two subjects helping the branch of growth economics advance as a more comprehensive subject.

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