

CCI Research Agenda
February 2022

I Theme Four **I**

Cultural Economics



CHARTER CITIES
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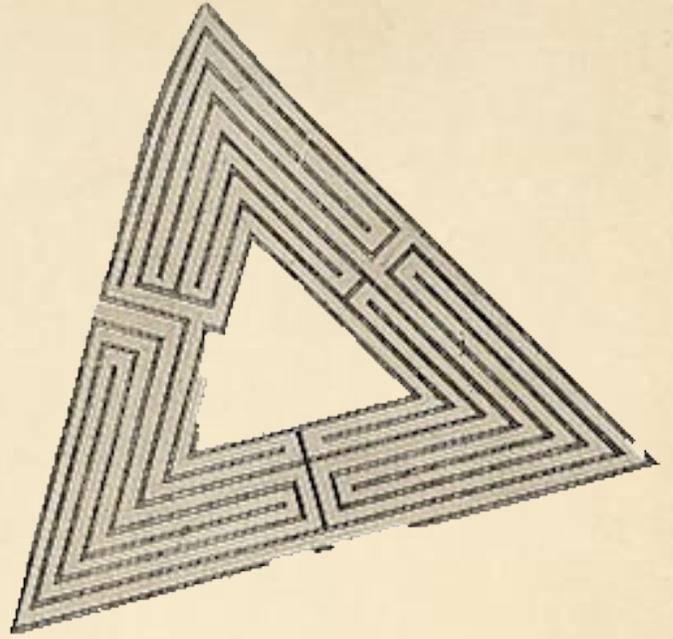
The Future of Development

Empowering new cities with better governance to lift tens of millions of people out of poverty.

The Charter Cities Institute is a non-profit organization dedicated to building the ecosystem for charter cities by:

- Creating legal, regulatory, and planning frameworks;
- Advising and convening key stakeholders including governments, new city developers, and multilateral institutions;
- Influencing the global agenda through research, engagement, and partnerships.





Culture, Institutions, and Economic Development

Few would doubt the influence of culture in economic development. Culture shapes our perceptions of the world, the choices we make, the ways we behave, and the institutions we form. This in turn determines our economic well being and history. However, despite culture's relevance to development, the phenomenon has been difficult to study. "Culture" is a theoretically fraught construct, and studying it within the standard economic framework raises a number of issues.

First, how do we define "culture" in an analytically meaningful and theoretically consistent way? Culture arguably encapsulates a vast set of distinct human characteristics, including "values," "beliefs," "traditions," "history," "law," and "preferences." However, casting a wide definitional net would yield a more accurate but less useful theoretical framework. If culture includes "everything," then it explains nothing. Social scientists continue to debate which features are most crucial in understanding the relationship between culture and development (Alesina & Giuliano, 2015), with many adopting the definition suggested by Guiso et al. (2006): "those customary beliefs and values that ethnic, religious, and social groups transmit fairly unchanged from generation to generation."

Second, the study of culture faces methodological ambiguities. Foremost, how do we measure and quantify culture? More subtly, how do we empirically identify the direction of its relationship to development? Culture is endogenous, meaning it both shapes and is shaped by the

institutional context. This ambiguity means that naive observations of culture may obscure deeper mechanisms of geography, law, history, climate, or even accidents. A classic example of this pitfall is the analysis of colonial institutions on development; was it the formal institutions established by European colonizers or the specific European cultural values underpinning them that determined modern wealth levels in postcolonial states (Acemoglu et al., 2001; Dzionek-Kozłowska & Matera, 2016)?

Third, cultural explanations of development can lead to normatively problematic conclusions. At its worst, such research can imply a hierarchy of cultural traditions (Landes, 2000). Overtly cultural interpretations of development lend themselves to erroneous claims of cultural "weakness" in the Global South. Scholars have also levied pragmatic critiques. Critics say that even if we can identify a robust causal effect of culture on economic outcomes, that may not help us generate policies to improve the world. Culture after all, is difficult to change.

Over the past 10 to 15 years, however, cultural economics is once again at the forefront of development research (Economist, 2020; Acemoglu & Robinson, 2021). This follows from the adoption of new empirical methods and the availability of richer datasets that allow economists to more rigorously interrogate cultural phenomena. A particularly rich source of information has been the World Values Survey, which

collects annual nationally-representative surveys in almost 100 countries. This has allowed social scientists to trace how culture and beliefs change over time (e.g., Matei & Abrudan, 2018; Minkov & Blagoev, 2009).

Research interest also arises from a change in mindset. The purely economic, a historical, and culture-agnostic approach to development has failed to fully explain real-world observations and broad historical trends (Nunn, 2020; Harrison, 2000). This approach also led to a “one-size-fits-all” style of policymaking, in which successful Western solutions were exported to the Global South. If culture doesn’t matter, then good policies should be easier to generalize to other contexts. However, failures in generalizing development policies have demonstrated the importance of understanding cultural context. Last, theoretical advances in behavioral economics, as well as a number of empirically-validated interventions, have made many economists and policymakers more optimistic of our ability to affect culture with policy.

The “new cultural economics” agenda differs markedly from the relatively absolutist approach of classical cultural works, in which cultural traditions were framed as “grand” determinants of social outcomes (e.g., Max Weber’s *The Protestant Ethic and the Spirit of Capitalism*, Samuel Huntington’s *Clash of Civilizations*, Lawrence Harrison’s *Underdevelopment Is a State of Mind*). It also expands on prior research on institutions, in which institutions were treated as blackbox catchalls for both

formal rules and informal (i.e., cultural) factors (North, 1991; Acemoglu et al., 2004). Instead, recent works focus on culture as a distinct variable of analysis that may interact with formal institutions to affect development. Likewise, culture is increasingly examined through its constituent parts (e.g., trust, gender norms, family ties, etc) rather than as a comprehensive hardwired tradition. Bisin and Verdier (2017) characterize this trend as a shift from studying the “proximate” factors of growth to the “deep” factors. Specifically, scholars are interested in understanding how institutions shape culture, how culture influences institutions, and how specific cultural traits affect economic choices and their impacts.

In the historical literature, cultural economists have attempted to isolate how institutions can shape culture in the long-run. Lowes et al. (2017) for instance, show how formal institutions may cause weaker social norms. They find that modern descendants of people living in the Kuba Kingdom, a 17th century Central African state with relatively formal legal institutions, were more likely to cheat than those who descended from people living right outside the kingdom’s boundaries. Their model argues that the existence of formal institutional constraints reduces the incentive to develop cultural norms that internally restrict undesirable behavior. In another study, Alesina et al. (2013) connect modern cultural beliefs about the acceptability of female participation in the labor market to pre-industrial agricultural practices. Regions that historically relied on plough

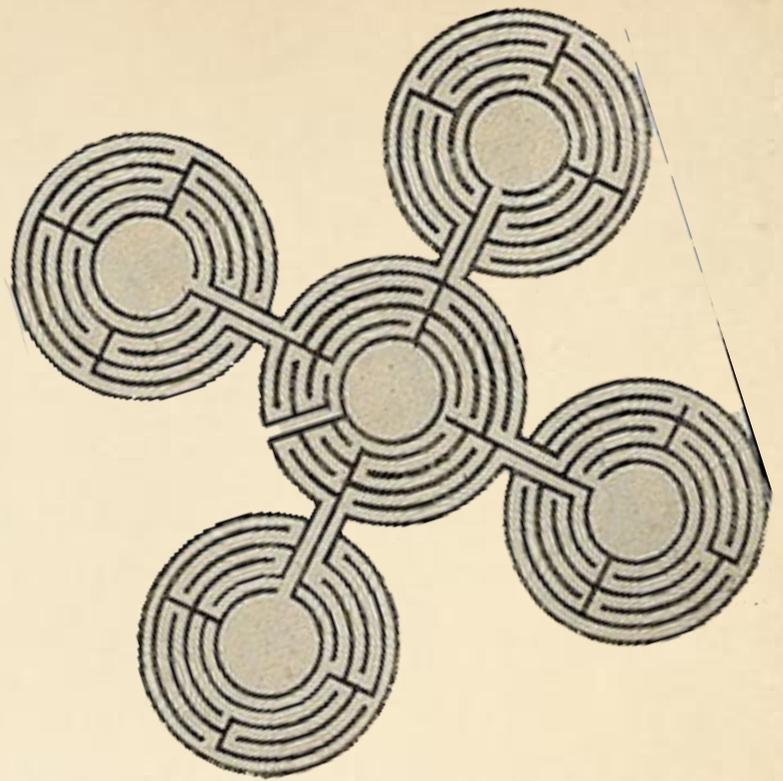
agriculture, which is relatively physically demanding, had divided labor participation along gender lines. These gender norms persist even in the modern economy. Nunn (2020) and Spolaore and Wacziarg (2013) review further research along this thread. What they show is that contemporary economic behavior is not solely shaped by pure economic incentives or short-term trends. Instead, they are strongly determined by persistent historical experiences that, as Nunn warns, cannot be ignored when designing policies.

The opposite relationship—how culture determines institutions—has been explored as well. This research question attempts to address a key skepticism in the institutional literature. Namely, do institutions matter as much as we think, or are these institutions just functional tools for culture? To summarize a few examples: Gorodnichenko and Roland (2021) use an instrumental variable approach to estimate the effect of individualism on democracy. They find that a one standard deviation increase in national individualism was associated with a four point increase in the Polity IV democracy index. In contrast, more collectivist cultures were more likely to experience autocratic breakdown. In a classic book, Fischer (1989) traces how the cultures of different groups of British colonizers influenced the institutions formed in America. For instance, Quaker settlers helped shape the industrial culture of the Mid-Atlantic. Guiso et al. (2004) find that Italian regions with greater social capital and trust have higher access to institutional finance, including household access to formal banking and firm access to credit.

The other relevant question is how does culture affect development? This line of

inquiry has tended to focus on how individually-measured beliefs and values translate into general economic behaviors. Much of the literature has also utilized methods from experimental and behavioral economics to more rigorously estimate causal relationships within a lab setting. Unsurprisingly, perhaps the most studied cultural trait in economics is trust; as Arrow (1972) writes, “Virtually every commercial transaction has within itself an element of trust, certainly any transaction conducted over a period of time. It can be plausibly argued that much of the economic backwardness in the world can be explained by the lack of mutual confidence.” Karlan (2005) for instance, finds that those identified as “trustworthy” in a standard experimental Trust Game were more likely to repay loans to a Peruvian microcredit organization.

Researchers have also explored broader cultural traits. Bertrand and Schoar (2006) used national survey data to look at the relationship between family structure and industrial organization, and they find that cultures with strong family ties have more family-run firms (as opposed to meritocratic or impersonal firms). As the authors argue, this may be bad for development as family firms are more likely to be corrupt, to remain small, and to operate less efficiently. Kafka and Kostis (2021) further examined culture from a perspective of change. They find that a shift in European values from “materialism” to “postmaterialism” over the past two decades was associated with lower economic growth. For a more exhaustive review of studies exploring culture and development, see Alesina and Giuliano (2015) and Algan and Cahuc (2014).



Cities and Cultural Change

Arguably, one of the most important drivers of cultural change is the city. By agglomerating people into densely-populated urban environments, cities accelerate the exchange of ideas and facilitate the formation of social networks. This can give rise to lasting prosocial cultural norms that minimize the frictions of urban crowding. Evans (2019) for instance, conducted fieldwork in Cambodia to see how cities affect gender norms. She argues that by offering women more career opportunities, cities raise the

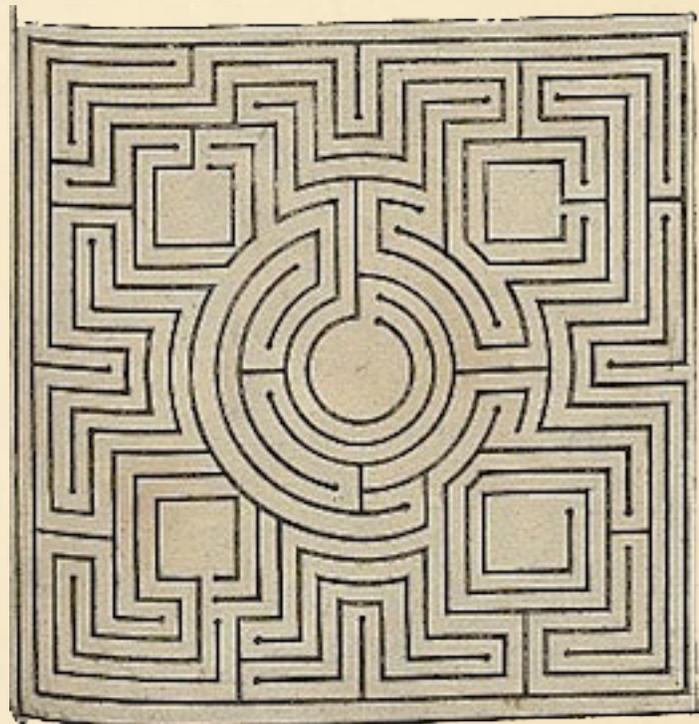
opportunity cost of gender discrimination. Similarly, Glaeser and Steinberg (2016) theorize that city-living builds “civic capital.” They argue that given the relatively cosmopolitan nature of most cities, urban residents must “consciously invest in their ability to deal with different people in order to take advantage of the opportunities.” The crucial mechanism is the deep incentive to form personal connections with others in society. This consequently leads to a more cooperative, inclusive, and “democratic”

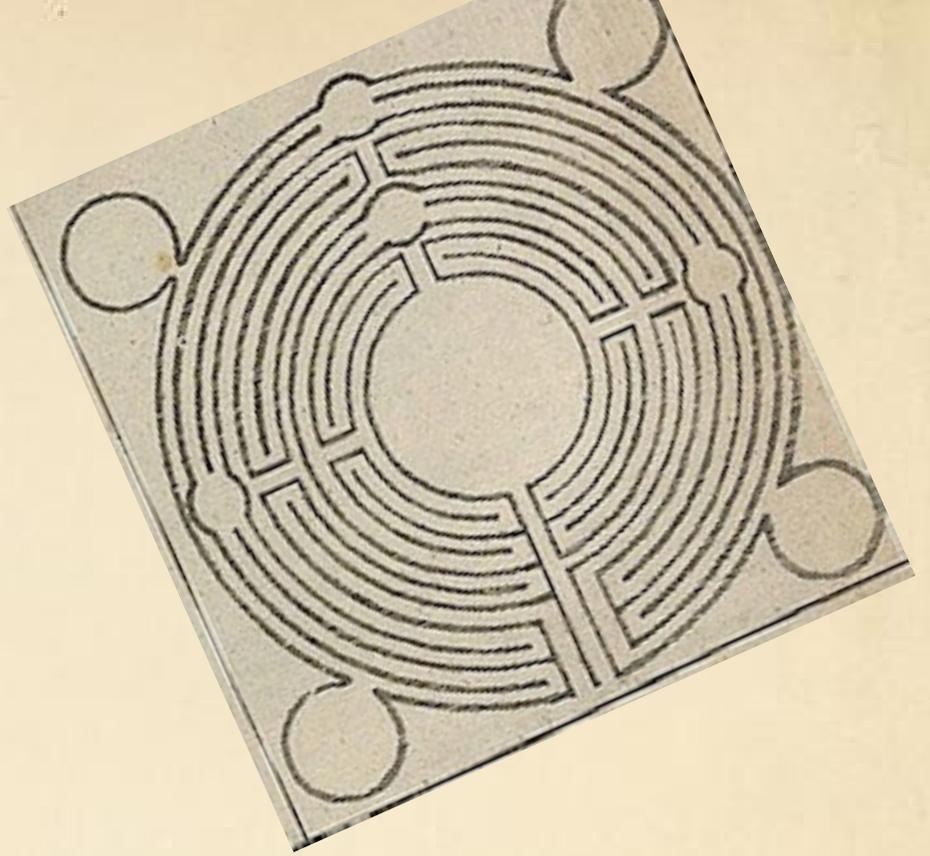
social equilibrium (Fosset & Kiecolt, 1989; Abrahamson & Carter, 1986). It also recasts the city as a cultural community beyond just physical boundaries (Post, 2018).

Perhaps the most seminal evidence for the cultural impact of cities comes from Putnam et al. (1993). They analyze differences in social capital and trust across 20 regions in Italy, and find that higher social capital led to better governance in North-Central Italy. The key insight is that modern regional variation in social capital (and ergo, governance) is a direct consequence of whether a region had free cities in the 12th century. Free cities were independent and self-governing medieval cities that exercised a form of early participatory democracy. This urban governance structure, Putnam et al. argue, encouraged citizens to develop a culture of belonging and civic community that remains today.

In other words, historical experience with specific urban civic institutions can translate to broader cultural changes that have significant consequences for economic wellbeing. This theory has since been formally validated by Guiso et al. (2016).

Miguel et al. (2003) extend the Italian mechanism by documenting a case of rapid social capital formation. They find that place-based industrialization in Indonesia from 1985-1997 led to more NGOs and community groups, higher rates of elders living with children, and lower rates of divorce. However, in contrast to Putnam et al., they find that baseline social capital did not predict industrialization in Indonesia within the study's timeframe.





Further Research

The optimistic relationship between cities and cultural transformation quickly breaks down in the Global South. Unlike Western cities, those in Africa, Latin America, and Asia are often marked by disease, slums, crime, informality, and disorder. D'Aoust et al. (2017) and Venables (2017) point out that African cities are prohibitively costly and spatially disconnected, which prevents industrial agglomeration and the creation of an urban market of ideas. This poses a

problem for rapidly urbanizing regions in the developing world, where cultural transformation is an important piece of the complex economic development story. That is, African cities may settle into a low-trust and low-social capital social equilibrium that is self-reinforcing, whereas more effective cities settle into high-trust and high-social capital equilibriums that promote growth (Putnam et al., 1993).

Charter cities can offer a potential solution to this problem. As discussed above, culture and institutions are integral for economic development. The problem for weak institutional contexts, however, is that culture and institutions are mutually reinforcing; to change institutions, we need to change culture, and to change culture, we need to change institutions. Charter cities aim to break this cycle by planting the seeds of broad institutional and cultural change. Their new institutions can generate new social norms and in turn help foster a positively reinforcing cycle of growth. If successful, these norms will hopefully spread throughout the host country. This is not just a byproduct of charter cities, but a key logic. New institutions and governance models will ultimately fail if they are not compatible with the cultural context.

This model extends from Greif and Kingston's (2011) institutions-as-equilibria framework. This approach views institutions as self-enforcing expectations and an emergent consensus, as opposed to an exogenously imposed set of binding rules. The corresponding social equilibrium can arise from historical accident, as was the case for rules dictating which side of the road to drive on, or from cultural beliefs. Consequently, institutions change when the underlying social equilibrium is disrupted. The theory of change undergirding charter cities frames itself as the social disequilibrating shock.

Acemoglu et al. (2021) further argue that we should look at culture in terms of fluid "culture sets" with expansive attribute

configurations, rather than as hardwired traditions. They write, "the same culture set can generate many different cultural configurations, each legitimizing and supporting a different type of political arrangement." An obvious case is modern China, which has arguably found a way to integrate into the global "Western" economy without overtly Westernizing its culture. Anthropologists also have a rich literature studying the mechanisms of "glocalization," in which global capitalist characteristics are reshaped to fit in with local culture (Roudometof, 2016). However, approaching cultural transformation and institutional development as such does have its pitfalls.

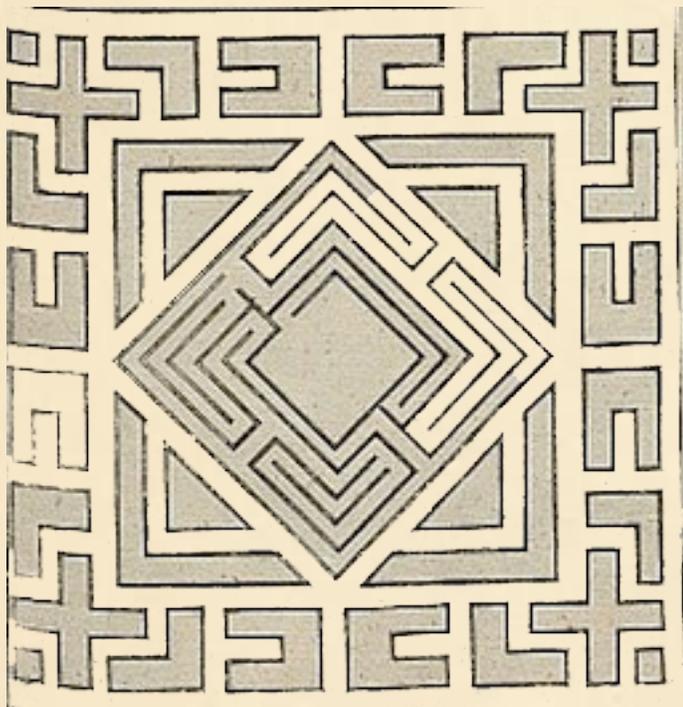
For instance, it opens up the discourse to heavy-handed claims that liberal democracy and liberal norms (e.g., gender equality, religious tolerance) are incompatible with certain cultures.

More ambitiously, we can also consider international "cultural spillovers." In some ways, the rapid development in East Asia can be seen as a story of international learnings. Lee Kuan Yew, for instance, has said that Japan's industrialization during the Meiji Restoration served as a roadmap for Singapore's transformation (Zakaria, 1994). Singapore in turn has become a model for many developing countries in Southeast Asia. Others have also pointed to the emergence of a global and universal liberal culture (Lopez-Claros & Perotti, 2014). Similarly, our hope is that charter cities can initiate broader regional change across the Global South, beginning at the local level of the city.

This is all to say that (1) cultural transformation is relevant for economic development, (2) many countries across the Global South are locked in a vicious cycle of bad institutions and growth-inhibiting cultural norms, (3) cities are promising agents for culture change, and (4) charter cities have a role to play in encouraging a new social equilibrium. This theory of change raises a set of research questions that require further exploration.

Examples of Research Questions:

- Do African cities incite or soften ethnic tensions?
- How have colonial institutions influenced modern trust?
- Do cultural traits affect urban crime across the Global South?
- Can cultural change minimize corruption? To what extent is corruption institutional or cultural?
- Can innovative forms of local governance (e.g., special economic zones, industrial parks, charter cities) result in more rapid cultural transmission?
- How does culture affect neighborhood characteristics and urban design?
- How important are social status symbols to urban development (e.g., car and home ownership)?



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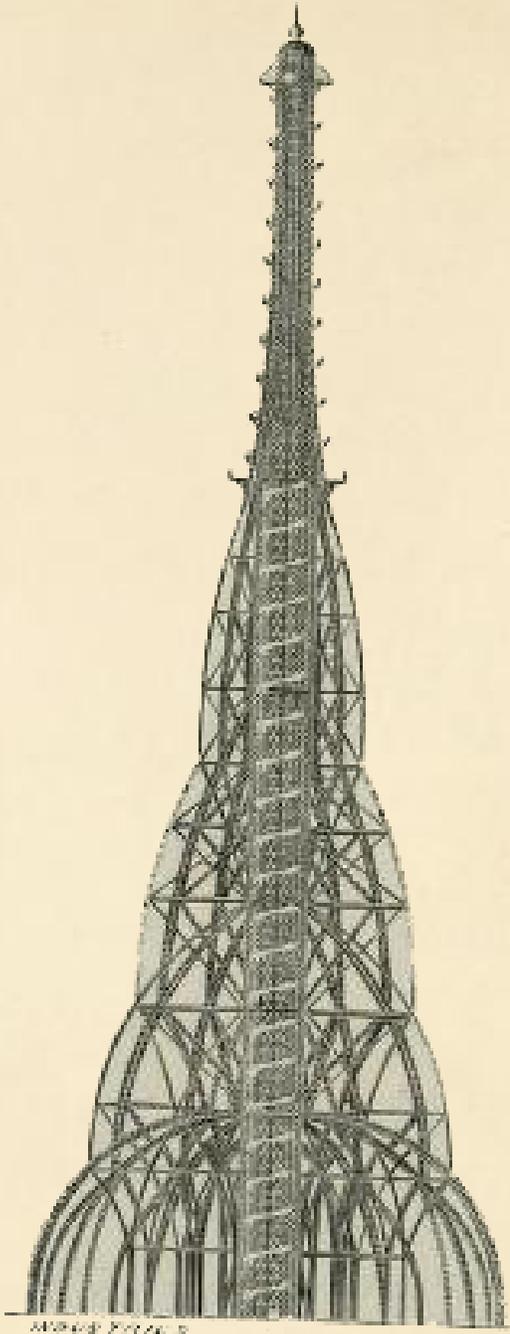
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