

Economic performance and culture in the view of economists. Critical observations from an action-theoretical perspective.

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Abstract

In neoclassicist explanations of economic performance actors are usually conceived as utility-maximizers, who make the „best“ use of given resources. Constraints are seen as originating mainly through the market or the legal situation. Neo-Institution-Economy (NIE) contrasts this view with the assumption that not only formal but also *informal* rules in terms of beliefs, values und norms must be an integral part of the model of the actor's behavior. This is the way in which culture enters the scene. One main argument developed in this essay is that important insights of the NIE-representatives are in danger of being compromised. This occurs where the reference to culture degenerates into „culturalism“. This essay envisages a possibility of escaping both the culture-blindness of the neoclassic economy as well as the culturalism of the NIE-exponents in a "balanced" conception of action.

Keywords: Neoclassic Economy, Neo-Institutional-Economics, culture, culturalism, balanced conception of action

The list of factors generally adduced by economists in order to explain economic performance on different levels of social aggregation contains very disparate elements. In it we discover phenomena such as techniques of production (Solow 1956), geographic location (Sachs 2003), physical and human capital accumulation (Romer 1986; Lucas 1988) or the quality of institutions (Baumol 1996; Gwartney et al. 2006; Dort et al. 2014; Acemoglu & A. Robinson 2012). Today, culture is also advancing to a prominent position as a variable which is intended to explain good or bad economic performance. This occurs not only with explicit reference to the term, but also by means of reference to concepts like „informal rules“ and „informal constraints“ (Williamson 2009), „mental models“ and „beliefs“ (North 1990, 2010; Greif 1994), „attitudes“ and „spirit“ (Landes 1998; Phelps 2006c), „narratives“ (Collier 2016; Schiller 2017, 2019) or „values“ and „norms“ (Sen 2001, 2004; McCleary & Barro 2001, 2002; Pejovich 2003; Guiso, Sapienza, Zingales 2006, 2007; Tabellini 2008, 2010; Shankha & Thompson 2015; Collier 2016; Nikolaev & Salahodjaev 2017). For a long time economists have virtually ignored culture as an important component of social life, mainly because they have ignored the role which generalized beliefs, values and norms play as components of human action. Especially in the neoclassical models individuals are not represented as moved by culture, but as actors who rationally maximize utility, making the best use of available opportunities. This situation has changed radically with the „neoinstitutional“ approach to economy (NIE).¹

Admittedly, institutions, not culture, contradistinguish NIE reasoning about economic performance. However, in the vocabulary of NIE, „institutions“ is a word which denotes different kinds of phenomena. In its *formal* occurrence this word refers *inter alia* to markets, bureaucratic and political arrangements, constitutions, or laws. Considered in their *informal* expression „institutions“ refer to generalized beliefs, ideologies, values, conventions, and internalized norms of conduct. Especially in this second meaning of the word, institutions are not supposed to be reducible to the optimization strategies of individuals. It is mainly through the insight that *qua informal rules* and *informal constraints* institutions condition people's choices that "culture" moves to the center of attention of NIE.

One main argument developed in this essay is that important insights acquired by NIE representatives are in danger of being compromised. This is especially true where reference to

culture degenerates into „culturalism“. With this term I refer to those approaches that conceptualize culture as a privileged determinant of action, without providing sufficient empirical evidence for this assumption. As we will see later in more detail, the problem with culturalism is not that it takes into account culture's influence on people's decisions, but that it portrays individuals as unable to articulate their own interests and to rationally exploit opportunities.

In this essay both neoclassical blindness to culture as well as NIE's propensity to culturalism are criticized and rejected. Both are unable to adequately represent the social actor in his efforts to make sense of the world and to act appropriately. In my perspective, an alternative to these positions can be identified in a „balanced“ conception of action. This amounts to a view which considers culture as an important dimension in human action, but at the same time rejects the idea that culture represents its main propelling factor. More specifically, „balance“ is attributed to a model of action, by which culture is considered as a dimension constantly „interacting“ with the actor's opportunities and interests. It remains an empirical question when determining which dimension acquires salience in the specific context of action.

The arguments in this essay are articulated in four steps: in *section I* I will contrast the neoclassical tendency to neglect culture as a important dimension of action with the NIE view, that considers culture as a necessary element in order to explain economic behaviour.² In *section II* I deal with the question of culturalism and ask to what extent NIE tends towards it. As I will argue, NIE's propensity for culturalism has many faces and appears in different degrees: whereas some NIE-representatives try to overcome the culture-blindness of neoclassicists making wide concessions to culturalism, others display a more cautious relation to culture as a determinant of action. Departing from the assumption that the alternative to culturalism cannot be a return to neoclassicist hypotheses, in *section III* I argue in favour of a „balanced“ conception of action. *Section IV* draws conclusions from the discussions of parts I, II and III.

Finally, two qualifications must be made. This essay does not aim to give a comprehensive picture of the scientific discussion on the relevance of culture for economic performance; it merely intends to consider the ideas of a number of prominent authors belonging to the economist camp. This does not mean that I could not benefit from the works of authors with a different disciplinary background, especially sociologists. Second, the essay does not intend to offer a general solution to the question of explaining economic performance, it merely seeks to discuss critically some assumptions of scientists who advance this claim. This does not imply that questions concerning explanation are completely passed over.

I) Differing approaches to culture

Exponents of neoclassic economy are not exposed to the danger of culturalism for the simple reason that culture plays little or no role in their explanation strategies. Scientists who emphasize parsimony in the construction of theoretical models avoid concepts characterized by high semantic diffusivity, such as „culture“. Deterministic implications must also be considered: understood as a determinant acting behind „people's back“, culture stands in blatant contradiction to the conception of an alert, rational and autonomous individuals that characterizes neoclassical reasoning. In the neoclassical paradigm, if conformity with shared cultural beliefs and values is considered, this has to be intended as the result of a cost-benefit calculation. For neoclassical economists, what in the end propel human action are not cultural values but individual welfare. As Gary S. Becker puts it, „individuals maximize welfare *as they conceive it*, whether they be selfish, altruistic, loyal, spiteful, or masochistic. Their behavior is forward-looking, and it is also assumed to be consistent over time“ (1993: 386).

NIE representatives do not agree with the view that individual choices always reflect substantive

rationality. There are, of course, situations in which this assumption seems appropriate. However, these are cases in which the competitive environment is relatively transparent for the actor: situations in which choice is repeated, trustworthy information can be easily obtained and rapid feedback allows for corrections of previous decisions. Matters are different in *complex* situations, situations in which choice is infrequent, direct experience is not possible or rare, and information about outcomes is limited and difficult to obtain. Under conditions of uncertainty, substantive rationality does not seem to be an appropriate option for describing or predicting human action.

With this problem in mind, how can we explain the fact that individuals are able to make decisions even in situations characterized by high complexity and uncertainty, situations in which the actor's rationality does not provide any indication how to behave? In order to answer this question NIE representatives resort to concepts like „institutions“, „formal“ and „informal“ rules, „mental models“, „ideologies“, „beliefs“ and „beliefs systems“. It is not easy to follow NIE exponents in their attempt to illustrate the intricate relations undergoing between these concepts. Let us try to untangle the knot by starting with „institutions“.

One assumption that almost all NIE representatives share is that individual choice and human behavior in general, has to be considered in the context of social institutions, not in the abstract. In the view of NIE exponents, institutions matter because they shape the incentive structure of a society. As North (1990:25) asserts: „The consequent institutional framework by structuring human interaction, limits the choice set of the actors“. More specifically, institutions constitute a central element to understanding long-term economic performance insofar as they provide specific incentives for action: institutions can encourage productive activities for individuals and firms, or they can encourage predatory behavior such as rent-seeking, corruption and theft (Hall/Jones 1999:95). Most NIE representatives agree also with the assumption that good institutions are those that secure property rights as the necessary condition for economic growth. As North and Thomas (1973:8) put it, „(E)conomic growth will occur if property rights make it worthwhile to undertake socially productive activity“.

This picture becomes more complex as soon as we consider that for NIE-exponents institutions possess two faces; understood as „formal rules“ or „formal constraints“, they embrace, among other things, parliamentary systems, bureaucracies, constitutions, laws, property-rights, and markets. Considered in their *informal* manifestation, institutions are supposed to encompass socially transmitted beliefs, values, norms, conventions, as well as styles of behavior. In this second meaning of the word culture enters the scene. Considering the fact that – even in contemporary functionally differentiated societies – informal rules and informal constraints quantitatively (by far) exceed formal rules, social scientists as well as economists cannot ignore them, they cannot ignore culture. As North states, informal rules „come from socially transmitted information, which are part of the heritage that we call culture“ (1990:37).

An important insight of NIE-exponents is that no political or economic change can be achieved by acting exclusively on formal rules. History illustrates that nations striving for better economic performance and acting exclusively on formal rules usually fail (North 1990:92). As Mantzavinos, North and Shariq (2004:79) write,

Since policies consist of changes in formal institutions, but outcomes are a result of changes in both formal and informal rules ... learning more about the interaction between formal and informal rules is the necessary condition for improving economic performance.

However NIE-representatives also admit that to change informal rules is a difficult task. In their cognitive (beliefs) as well as in their evaluative (norms) and expressive manifestations (styles), informal rules possess a core that cannot be changed by political decree.

Against the background of these insights concerning content and function of informal rules, NIE

representatives can claim that the neoclassical view is reductive, insofar as it considers individuals as equipped solely with preferences and the disposition to maximize utility under the constraints of given prices and available income. What in this view is missed, is culture in the form of informal rules and informal constraints.

Admittedly, not all NIE representatives operate with concepts like „informal rules“, „informal constraints“ or „culture“. It is also true that NIE representatives discovered the analytical virtues of these concepts relatively late. In Oliver Williamson's (1975) early work, for instance, the main question is how hindrances for cooperation can be brought under control. Williamson does not answer this question with reference to informal rules or to culture, but with reference to governance structures able to reduce the negative effects of opportunism and malfeasance. Only in Williamson's late work (2000) is culture decidedly brought to the center of attention. In his attempt to identify important determinants of human action, Williamson proffers a four-level ladder in which the elements of the higher level are seen as constitutive for the elements of the next lower level. At the summit of this ladder, Williamson locates „informal rules“. These are constitutive of and causally connected to the elements immediately below, which Williamson identifies as „formal rules“. Formal rules, on the other hand, are supposed to provide structural opportunities as well as constraints for „institutions of governance“, located on the third level of the ladder. On the bottom of the scale we find prices which create structural conditions for the regulation of individual transactions. To distinguish between these four levels, Williamson also employs temporal criteria. Whereas changes in prices are constant, the change of institutions of governance may require decades. Whereas changes to formal rules require centuries, informal rules evolve in millennium rhythms.

An important question among NIE exponents is how informal rules conditioning the process of economic growth are generated and perpetuated over time. North (2010:83) gives an apparently simple answer to this question. Considered as conventions, values, norms or behavioral maxims, informal rules are generated and transmitted through generalized *beliefs*: „The key to building a foundation to understand the process of economic change is beliefs – both those held by individuals and shared beliefs that form beliefs systems“.³

The planning and implementation of reforms in the political and economic assets of societies cannot ignore collective beliefs.⁴ These are an important reference point in understanding or foreseeing the dynamics of societal and economic change. North writes:

We must have not only a clear understanding of the beliefs structure underlying the existing institutions but also margins at which the beliefs system may be amenable to changes that will make possible the implementation of more productive institution. Only then will we have a knowledge of the sources of the existing institutions, their organizational underpinnings, and insights into possible structural reform (North 2010:163-164).

In the view of some NIE representatives, generalized belief systems are supposed to set the course for future developments, they create „path-dependence“. In North's definition (2010:52) „(p)ath dependence indicates the constraints on the choice set in the present that are derived from historical experiences of the past“: path-dependence means the creation of self-reinforcing mechanisms. Where „increasing returns“ or high "exit-costs" are expected, path-continuation and the activation of „lock-in“ mechanisms will follow: the accidentally started path solidifies in a structure with consequences on present and future development. Under path-dependent conditions, options for choice are supposed to be very limited.

NIE exponents usually assume that societies exhibiting similar formal rules, resources, prices and preferences, but differing in path-dependence, will diverge substantially in their political and economic performance. To state that generalized beliefs generate path-dependence is another way of saying that culture in its cognitive manifestations conditions present and future events.

The assumption that „... the tension between altered formal rules and the persisting informal constraints produces outcomes that have important implications for the way economies change“ (North 1990:45) has been of great relevance to later research on economic performance. Pointing at social and economic changes in Eastern-European countries, Steve Pejovich intends to offer an empirical proof of this assumption. Pejovich sees the degree of tension between newly established formal rules and the existing informal rules as a key element for understanding the process of transition to democracy and to a free market economy. Pejovich's (2003:349) „interaction thesis“ postulates that:

When changes in formal rules are in harmony with the prevailing informal rules, the incentives they create will tend to reduce transaction costs and free some resources for the production of wealth. When new formal rules conflict with the prevailing informal rules, the incentives they create will raise transaction costs and reduce the production of wealth in the community.

According to Pejovich, in many former Eastern Block countries, two opposing cultures can be observed: on the one hand a „capitalistic culture“, characterized among others by a free market, individual performance, responsibility, open competition, and property rights, on the other hand a culture characterized by tradition, collectivism, egalitarianism, the welfare state, and insecure property rights.⁵ Pejovich's assumption is that transition-countries unable to reduce this tension, are doomed to pay high transactions costs in terms of the acquisition of information, negotiation, decision-making processes and monitoring of procedures.

Is traditional culture, are usual ways of thinking and behaving, as Pejovich seems to suggest, at any rate detrimental to good economic performance? Among NIE representatives and economists in general, not all agree with this assumption. As Senn (2001:5) observes with reference to non-western countries, there have been several different theories seeking explanation of the high performance of east Asian economies in terms of traditional values.

From this perspective it seems plausible to see economic failure as a consequence of the fact that individuals and groups abandon successful traditional paths. Eduard Phelps seems to endorse just this position when he identifies reasons for the poor economic performance of contemporary European nations. In Phelps' view, indicators like employment, productivity, export-rates and wages show unequivocally that, in comparison with countries like the USA and China, continental European countries are on the economic decline. To explain this fact, Phelps reverts not only to the poor performance of formal institutions or to the scarcity of natural resources, but also to the progressive disappearance of what he calls the „entrepreneurial spirit“:

... It is not obviously bad economics to admit the possibility that some economies, for example those of continental Western Europe suffer low entrepreneurial activity not solely because of poor profit prospects or, conceivably, poor financial institutions, but because they have a low level of ‚entrepreneurial spirit‘ (Phelps 2006c: 14).

In Phelps' (2005:5) view, in a not too remote past the „entrepreneurial spirit“ found expression in Europe in phenomena like innovation, dynamism, creativity, good quality of business life, and high worker motivation in the production process. These qualities have lost their power today, because the spirit that once sustained them has eroded. How could this happen? How could the „old values“ that gave supremacy to Europe lose their power?

Phelps believes to find an answer to these questions in that particular societal system adopted by many European countries in the time between 1925 and 1940, which he defines as that „corporatist mind set“ which have done great harm to Europe's dynamism and, in turn, „to its economic performance“ (2005:9). Following Phelps, corporatism, as a phenomenon characterized by social partnership, concertation, and co-determination, generates a situation in which private income and private ownership is retained, but the entrepreneurial spirit is discarded:

To the extent that a continental Nation retains vestiges of corporatist institutions and thinking, these causal influences may appreciably account – more than the nation's welfare states – for the alienation from business, the dearth of innovation, and therefore the apparently low levels of job satisfaction, the low participation and the generally high unemployment rates that have become familiar on the Continent (Phelps 2005:8-9).

Phelps' observations complement and at the same time specify the view of those scientists who believe that formal rules like company law, corporate governance, population preparation for business-life, development of financial instruments (stock market) and property rights, represent necessary but not sufficient conditions for good economic performance and economic growth. In addition to these formal rules we also have to consider the „entrepreneurial spirit“ as an expression of culture. In Phelps later work the view on culture as a privileged explanatory category remain unchanged. As he writes (2013:194), „as important as institutions and policies may be, we must recognize that every economy is a culture or mix of cultures, not just policies, laws, and institutions“.

In the discourse of distinguished contemporary economists trying to explain dysfunctional economy like depression or recession, we cannot forget those scientists like Schelling and Collier, who assume *narratives* as central reference point. With the expression „narrative economics“ Schiller (2017:967) understands the study of the spread and change of popular narratives in a specific community and how these condition economic fluctuations. Schelling's (2017:968) definition of narratives is simple:

I use the term narrative to mean a simple story or easily expressed explanation of events that many people want to bring up in conversation or on news or social media because it can be used to stimulate the concerns or emotions of others, and/or because it appears to advance self-interests.

As Schelling (2017:969) argues, narratives, as mental constructs which influences how causal relationship are understood or misunderstood, are acquired by people „through their immersion in a specific culture or social network“. Research on popular narrative is important, because it allow us to understand the genesis and development of significant economic events in our history. Looking at narratives Schiller (Ibid.:967) believes to reach a better understanding of events like the 1920-1921 Depression, the Great Depression of the 1930s, the so-called Great Recession of 2007-2009, as well as „the contentious political economic situation of today“.

Paul Collier's (2016:8) arguments about the power of narrative to condition people's action, und specifically economic action, are similar. He argues that, in addition to analytic explanation and direct observation narratives are important for the way in which people acquire understanding of causal processes. For Collier (2016:8-9) a society with a strong cultural disposition to the narrative of fatalism, „for example because its members have experienced failure and so find loss-aversion particularly attractive, will thereby be characterized by lower efforts than a society characterized by a narrative of opportunity“. But for Collier narratives are also important in order to understand the ability of countries to attract finance capital. As Collier argues, one reason why Africa has failed in this respect is that „the prevalent narrative discourages making deals with foreign companies. Transactions are commonly seen as being zero sum games, and a legacy of colonialism is that foreigners are widely seen as exploitative“ (Collier 8-9).

Our list of selected scientists who put culture at the center of attention can, without any pretense of completeness, be complemented by research-trends (Guiso, Sapienza, Zingales 2006; 2007; Tabellini 2008; 2010), mainly based on statistical analysis. Following a line of research inaugurated by Robert Putnam *et alia* (1993) in his investigation of Italy's political and economic divide between the South and the North, Tabellini (2008; 2010) emphasizes the strong correlation between economic growth on the one hand and phenomena like „social capital“, „generalized morality“ and

„trust“ on the other hand. Tabellini shows that in many cases this correlation is mediated by institutions: high levels of trust and morality correspond to high quality levels of governance and institutional performance which, in turn, correlate strongly with economic growth. Considering the presence of almost *identical* institutions on the national level, what could explain the marked differences of performance between the North and the South of the Italian peninsula? Using a multi-regression approach Tabellini (2010) does not hesitate to answer this question with reference to culture. Culture is supposed to explain why relatively inefficient economies persist even when the institutions of the more efficient economies have been adopted. Cultural factors seem to account for the fact „that economic and policy outcomes are very persistent, and often remain unaffected by sudden changes in formal political institutions“ (Tabellini 2010:256). In short, culture matters.

II) Between cultural irrelevance and culturalism

As we saw, NIE representatives refer in different ways to culture: as „informal constraints“, „internalized values“, „norms“, „generalized belief system“, „mental models“, „path-dependence“, „entrepreneurial spirit“ or „narratives“. In contrast with neoclassical economists, proponents of NIE consider culture to be an important determinant of human action, and by extension, as a relevant factor in explaining economic performance. The trouble with this view is that it proffers too many concessions to „culturalism“. In order to illustrate this, let us return briefly to the aforementioned authors.

Williamson's four levels of analysis do not claim to offer a classification of *empirical* phenomena. However, upon closer consideration, it cannot be denied that Williamson attributes to culture a factual determining power over all other factors. As Williamson says, informal rules display a „lasting grip“ on the organization of entire societies (ibid.:3). Moreover, Williamson does not seem to have appropriately considered the possibility of feedback between the elements of the ladder. He does not consider the possibility that, even in the long run, changes in formal rules could have an influence on informal rules.

As we saw earlier, North also attributes to culture a prominent role by the explanation of economic performance. North's (1990:92-93) main questions are: What accounts for the survival of societies and economies that are characterized by persistent poor performance? Why do relatively inefficient economies persist? What prevents them from adopting the institutions of the more efficient economies? As mentioned previously, North answers these questions with reference to concepts like informal rules, mental models, beliefs and ideologies. This fact alone surely does not allow us to place North in the group of the culturalists. But neither can we assert that he can be totally excluded from this group. The concepts of „beliefs“, „mental models“ and „path dependence“ aptly illustrate this point.

Following Denzau and North (1994:4), one main function of mental models is to articulate predictions and expectations regarding the environment. If a mental model is repeatedly confirmed, it becomes a stable acquisition in the individual's stock of knowledge. When this happens, the mental model acquires the status of a „belief“ or a „belief system“:

When environmental feedback confirms the same mental model many times, it becomes stabilized, in a way. We call this relatively crystallized mental model a "belief"; and we call the interconnection of beliefs ... a "belief system" (Mantzavinos, North, Shariq, 2004:76)

Considered as the product of people's experience with their environment, mental models differ from individual to individual.⁶ This specificity of mental models turns communication into a problem. How is communication possible among individuals with different mental models?

In order to answer this question, North et al. resort to culture. It is culture in terms of shared beliefs and ideologies which is supposed to provide a common background for communication and interpretation of the world: „The cultural heritage provides a means of reducing the divergence in the mental models that people in a society have and also constitutes a means for the intergenerational transfer of unifying perceptions“ (1994:15).

North assumes that, depending on the fact that people's expectations are validated by the environment, mental models are confirmed, revised, refined, or rejected altogether:

When a solution produced on the basis of a certain mental model has not succeeded, an individual employs inferential strategies - especially analogies - in a quasi-automatic way. If these strategies do not solve the problem either, then the individual is forced to become creative - that is, to form new mental models and try new solutions (2004:76)

However, at the same time North seems to deny the possibility of revising given mental models the moment the learning process is conceived as „a function of the way in which a given beliefs system filters the information derived from experiences“ (North 2010:69). North's argumentation appears to be not quite consistent. On the one hand, he considers learning through feedbacks as possible and necessary in order to initiate change, on the other, he conceives of learning as functional to existing belief-system. In light of existing belief-systems as powerful „filters“ of incoming knowledge, it may be asked, how effective learning and real change could be engendered.

Similar considerations can be made in relation to North's use of the concept of „path-dependence“. Considered as an analytical tool to explain the persistence of inefficient equilibria, path dependence can offer valuable services to the researcher. It provides an answer to the familiar observation that inefficient or suboptimal resource allocations can persist over time and are difficult to change. With reference to path-dependent mechanisms, we can make sense of the fact that interaction between rational actors does not necessarily lead to optimal results. On the other hand, path dependence emphasizes past events as a cultural burden which imposes heavy constraints on present actions. As North states:

We have now come to understand enough about institutions to be able to pinpoint the sources of poor economic performance. They have their origins in path dependence. We inherit the artifactual structure - the institutions, beliefs, tools, techniques, external symbols' storage systems - from the past. ... The degree to which such cultural heritage is "malleable" via deliberate modifications is still very imperfectly understood. At any time it imposes severe constraints on the ability to effectuate change (North 2010:156).

As an analytic instrument which focuses on constraints generated by history and culture, path-dependence is basically oriented to detect reasons which push individuals to perpetuate inefficient behavior. The path-dependence approach is not oriented to detect actors' efforts to come to terms creatively with their natural and social environment. As has been critically observed (Crouch & Farrel 2004:16), „Path dependence ... seeks explicitly to model circumstances in which early events increase the possibility of later events of the same sort occurring“.

In North's argumentation sometimes a second use of path-dependence can be observed: in society there are „powerful“ actors, who have a pronounced *interest* in perpetuating familiar paths, and there are also „weak“ actors, who have an explicit interest in changing the path, but do not have the resources to do so. However it is the understanding of path-dependence as systemic inertia and ineluctability, which in North's view seems to prevail.

How cultural beliefs, informal constraints or path dependence are transformed from useful analytical tools into ineluctable traps can be illustrated with reference to Pejovich's analysis of former Eastern-Block States. For Pejovich (2003) the reasons for the failure in the transition to capitalism in C&EE (Central and Eastern Europe) must be sought in culture: „transition is a cultural

problem“ (Pejovich 2003:358).

Pejovich's conception of the social actor seems to fluctuate between two extremes: on the one hand, this actor is seen as self-determined, rational, calculating, and able to recognize own interests and to exploit existing opportunities. On the other hand, this actor is considered to be completely emerged in a specific culture (as national culture) in a way that the alteration of old formal rules and the creation of new opportunities will have little chance of prevailing:

New formal rules create new incentives and opportunities for human interaction. How individuals react to those new opportunities for exchange depends on how they perceive them. And how individuals perceive new opportunities depends on the prevailing culture (ibid: 348).

How culture acquires the status a privileged variable can also be observed in Phelps' approach to economic performance. It would be a mistake to consider this author *tout court* as a culturalist. Nevertheless, in Phelps' argumentation too, we can identify a clear propensity to culturalism. This is for instance the case, when he discusses the sources of prosperity. He (2005:5) asks, „(W)hat is the main source of the prosperity deriving from a nation's economy? Is it certain economic institutions – the presences of some and the avoidance of others? Or is it culture? Or what? Or is it maybe a vast panorama of things?“ A balanced answer to these questions would not favor culture at the cost of institutions. However, in this regard Phelps (2005:11) seems to endorse a different view⁷:

We may find that institutions choices by countries appear to be the cause of differences in economic performance but these institutional differences across countries are mere reflections of differences in culture whose primary influence is direct, not through institutions.

Also Schiller's view of culture as „popular narrative“ is not free from ambiguities. As Schiller (2017:968) admits, „we cannot easily prove that any association between changing narratives and economic outcomes is not all reverse causality, from the outcomes to the narratives.“ Moreover, what seems to speak against the culturalist view is also the observation that „stories tend to be strategic“ (Akerlof and Schiller 2015), that „much of the purposeful generation of new stories is for individual profit“ (Schiller 20017:979), and that „among normal people, narratives are often somewhat dishonest and manipulative“ (ibid. 969). These instrumental views make the hypothesis plausible of narratives as intentional constructions which influence culture, not the other way round:

Narrative are major vectors of rapid change in culture, in zeitgeist, and ultimately in economic behavior. Spreading narratives, often many parallel narratives around a common theme have been creating cultural change long before the internet revolution... (ibid. 973)

However the foundation of narratives in culture is also asserted by Schiller. This becomes evident when the „unconscious“ and „pre-rational“ acquisition of narratives is emphasized.⁸ This becomes also evident when Schiller (ibid. 967) assumes that „sometimes the dominant reason why a recession is severe is related to the prevalence and vividness of certain stories, not the purely economic feedback or multipliers that economists love to model.“

The considerations made above shows that NIE representatives do not speak in unison. Within (and outside) the heterogeneous NIE camp, it is possible to identify voices which articulate a reserved, or even critical view of culture as an explanatory variable. Acemoglu and Robinson (2012:57) ask: „Is the culture hypothesis useful for understanding world inequalities?“ In conformity with basic assumptions of NIE, they emphasize the fact that the explanation of institutional and economic differences requires reference to norms and values. They also admit that „social norms, which are related to culture, matter and can be hard to change“ (ibid.). However, both authors hasten to emphasize that in the most cases, cultural factors „are just not important for understanding how we got here and why the inequalities in the world persist“ (ibid.). To explain economic performance,

Acemoglu and Robinson prefer to resort to phenomena like cooperation and trust, underlying the fact that both factors must be considered as products of the function of institutions and not of culture (ibid.).

Scepticism about taking culture as the main *explanans* for economic performance is also expressed by Mancur Olson (1996). He rejects the assumption that countries are poor because the people lack specific cultural traits. In other words, he (ibid.:15) refuses the assumption that people „... have the ‚Protestant ethic‘ or other cultural or national traits that are supposed to make them hard workers, frugal savers and imaginative entrepreneurs“. With an eye to international migration, Olson produces evidence for the fact that not culture, but institutions are the best candidate to explain national differences in economic performance:

Newly arrived immigrants ... have approximately the same marketable human capital or personal culture they had before they migrated, but the institutions and public policies that determine the opportunities that they confront are those of the host countries" (ibid.:16-17).⁹

Amartya Sen (2001), another author with loose affiliations to NIE, also argues against culturalistic explanations of economic performance. Following Sen, in explaining human action, scientists have to avoid both extremes: those which deny culture of any relevance and those which attribute to it the main power among all possible determinants. As Sen writes,

In assessing the cultural influences on values, behavior and performance, we have to avoid both the insular thesis that culture makes no real difference and the over-grand theories that allegedly explain the major contrasts in economy, politics and social performance across the world entirely - or mainly - in terms of cultural differences (Senn 2001:11).

Authors like Acemoglu and Robinson, Olson and Sen recognize the danger in explanation strategies which conceive culture as the main variable at stake. At the same time, they attribute to culture an important explanatory function. One can surely agree with this view, but we may still ask which model of action is appropriate to support the view that culture matters, but is not always the main power at stake. As I argue in the next section, the answer to this question needs to be sought in a „balanced“ conception of action. Equipped with the insight that the basic analytical unit for social scientists as well as for economists are individuals and their actions and interactions, these two categories move to the center of attention.

III) Basic characteristics of a balanced conception of action

As already mentioned, among economists culture could emerge as an important analytic dimension in the measure in which the limits of neoclassical thinking became evident. Many factors contributed to the insight that understanding economic performance culture matters.

Very early criticism has been addressed to the neoclassical assumption of a social actor, who pursues individualistic aims against the background of optimal knowledge about existing alternatives, an actor whose utilities are both known and constant (Stigler and Becker 1977). This assumption may be appropriate for situations in which the choice is simple, when it is repeated in time and rapid feedbacks are possible. However, as critics have emphasized, people's important choices are infrequent and knowledge about possible outcomes is mostly unknown or difficult to obtain. As Phelps (2006a:4) puts it, „the neoclassical framework with its premise of perfect knowledge and perfect coordination is too narrow for much understanding of underperformance and the possible role that institutions and culture may play in it; so we want to go beyond neoclassical economics.“ „Bounded rationality“ (Simon 1993; Gigerenzer, Selten 1999) has consequences regarding the question of economic performance.

Of course, going beyond neoclassical economics implies more than just recognizing that the actor's rationality is bounded. It also implies realizing that the assumption of the human actor exclusively concerned with future events („forward-maximizer“) is too narrow.¹⁰ This assumption does not consider that „backwards-looking“ (Macy 1993), in terms of orientation to tradition and custom, as well as „sideways-looking“ (Hackathorn 1996), in terms of orientation to habit and conventions, may represent important orientations for the actor's action.

Furthermore, going beyond neoclassical economics means recognizing that economic behavior is always embedded in social relations. Economic sociology has emphasized that the neoclassical view operates with an atomized, undersocialized conception of the human actor (Granovetter 1985). This view is unable to account for the fact that patterns of social relations are important in order to understand economic transactions and their outcomes. Neoclassical thinking focuses mainly on the individual interests of the actor and tends to neglect the impact of horizontal and vertical interpersonal relations on economic action. In other words, it underestimates the role of norms like trust and cooperation as well as power and compliance (Granovetter 2000:350-351).

Finally, going beyond the neoclassic paradigm means realizing that the assumption of utility-maximization as the paramount criterion for modelling action is misconceived. If we consider seriously the actor's embeddedness in the social and cultural context, the attribution of „good reasons“ (Boudon 1996) is surely a better option as the attribution of a „strong rationality“: in certain epochs it is reasonable to believe that the earth is located at the center of the universe. Similarly, in specific cultural settings it is reasonable to believe in the power of magic. To the same order of reasoning belongs the observation that, whereas in specific social or cultural settings, personal profit-maximization may be opportune and even desirable, in others it is not. Societies and groups have different views concerning where these spaces are located, which extension they have and how clear their borders are (Beckert 2005:11).¹¹

All these varied critiques of the neoclassical paradigm seem to converge on one point: in the form of individual beliefs as well as in that of norms and values, culture denotes a dimension of action which cannot be neglected by the attempt to understand people's behavior. However the danger in appreciating the relevance of culture in people's behavior is overestimating its power. This is especially the case whenever culture acquires the status of a privileged variable in the specific explanatory strategy. As we have seen, NIE exponents are exposed to these dangers in different ways and to different extents.

In Williamson's (2000:3) four-level ladder, in which the upper level imposes constraints on the next level below, we look in vain for influences going in the other direction. In this ladder the possibility that the introduction of new formal rules, can generate in the long run changes of informal rules (norms and values), is not considered.¹² A similar criticism also applies to North's argumentation, which starts out historically (1990) and then becomes more and more psychological (2010) in character. North's conceptual and methodological perspective („path dependence“, „mental models“, „beliefs system“) is more prone to restrict the space in which actors are supposed to move than to enlarge it. In addition, North's understanding of learning as a function of the way in which existing beliefs filter individual experience seems to degrade learning to a mere reiteration of past acquisitions. Looking at transition processes in previous Eastern-Bloc-States, Pejovich (2003:348) argues similarly: how actors react to the creation of new incentives „depends on the prevailing culture.“ In Pejovich's description neither people's interests (political elite) nor people's opportunities find adequate consideration. Had Pejovich dedicated more attention to interests, he would have realized that not only culture, but also the desire to avoid personal disadvantages induces people (older generations) to opt for the *status quo*. Similar considerations have to be made with reference to Phelps' approach to economic performance. Phelps (2006a:4) is surely right when he observes that with reference to the conception of actor of neoclassical economists, no appropriate

explanation of economic performance can be delivered. However, Phelps - even though he sometimes qualifies his argumentation with a „may be“ or a „perhaps“ - is wrong when he thinks to can explain it with a privileged reference to culture.¹³ Both neoclassical economists as well as NIE-exponents seems for different reasons not to rely on a balanced conception of action. To this problem there is more to be said.

Cultural values and norms are supposed to accomplish two important functions by the actor's attempt to articulate purposeful action: they enable the hierarchization of preferences and at the same time indicate how choices can be implemented. What appears questionable are not these two functions, but their overestimation. In particular three aspects must be considered: functional weakness, context-dependence and the underdetermination of values and norms.

Cultural values and norms are *functionally weak*. Taken alone they do not have the power to coordinate and direct people's action. If internalized cultural values and norms were sufficient to accomplish this task, control and sanction as instruments of *externally* regulating people's behavior would be superfluous (Lindenberg 1983:451).

Values and norms are *context-dependent*. As Amartya Sen (2001:8-10) observes in relation to the Japanese context, „the same values and cultural norms can be extremely successful at one phase of development, but less so at another.“¹⁴ The context-dependency of values is also illustrated by Experiments in game theory. They show that, depending on the actor's definition of the situation („framing“), choice can be selfishly or altruistically, cooperatively or uncooperatively oriented (Tversky and Kahneman 1981). There is a large database of experimental results in the area of trust, ultimatums, and social dilemma games, illustrating how small alterations in the environments, or in the way the game is presented, induce major behavioral changes: „Individuals may be cooperative on some occasions and selfish in others, give generously or reciprocate at times and be ‚mean‘ at other times“ (Bicchieri, 2006:46).

Finally, values and norms are *underdetermined* and sometimes even contradictory. In most cases they do not contain prescriptions regarding the way in which they could be implemented, or these prescriptions are not specific enough. The observations of Fredrik Barth (1993:35) in relation to a specific ethnic community holds true for all groups: „It is not that values cannot be found - it is rather as if ones finds a surfeit of them: too many, too discrepant, too often disconnected with any filled of effective choice, or applied as ways of speaking rather than action, and sometimes, but not always, increasingly vacuous and irrelevant the wider their scope and the more fundamental their pretensions“.

Functional weakness, context-dependence and under-determination of cultural values and norms cast doubts on the assumption that action is exclusively or predominantly determined by actor's internalized culture. Factual compliance to norms and values can be seen as the consequence of the fact that non-compliance implies high costs for the actors. Compliance can also be considered as a function of instrumental reasoning: cooperation and reciprocity occur not because they are imposed by culture, but because they turn out to be beneficial for individuals. Of course, we cannot exclude the fact that compliance to norms is also based on ethical principles. We cannot exclude that on the ground of ethical principles, person X will cooperate even when person Y does not.

However, culturalism is not only related to the conviction that action is driven by strong and unambiguous values and norms. Culturalism is also related to the assumption that values and norms are always primary or exclusive determinants of human action. What is neglected in this view is the power of *interests* or *desires* to shape human action.

The way that NIE representatives underestimate the power of interests or desires can, for instance, be observed in Pejovich's analysis of the transition to democracy and capitalism. As Pejovich (2003:352) admits, we have to take seriously the desire of people in C&EE countries to change the rules of the game. Furthermore, we need to consider the interests of the elites in perpetuating „the

collectivist mode of the accumulation of power and wealth“.¹⁵ However, the general tone of Pejovich’s argumentation is that it is culture as the collectivist mode of looking at world which in the context of different powers determines people’s behavior in C&EE countries: „their culture is the culture of collectivism and shared value. This means that they are evaluating the system they want to build through the lens of a different system“ (2003:15).

In order to account for the resistance to change, North (2010:157) refers to both, cultural beliefs as well as to people's interests. As he states, beliefs „are impervious to change either because the proposed changes run counter“ a given beliefs system, „or because the proposed alteration in institutions threatens the leaders and entrepreneurs of existing organizations“. However, by assuming that „the belief system underlying the institutional matrix will deter radical change“, North (2010:77) seems to resolve the tension between cultural beliefs and interest in favor of the first element.

The way in which culture governs people’s life is also illustrated by Phelps’ attempt to explain differences in the institutions of various countries. According to Phelps (2006a, 3), the reason for this difference is to be found not so much in the interests of some groups to maintain or not to maintain the *status quo* but in the prevailing culture, which cause them „to prefer a different system of institutions“. (Ibid.:3).

„Balance“ means avoiding both: models of action by which individuals are portrayed as only acting instrumentally, or conversely as blindly conforming to cultural values and norms. It is questionable, when in search for reasons for differences in economic performance, neoclassic economists resort to explanations based exclusively on interests and opportunities, thereby underestimating the role of culture.¹⁶ Likewise, it appears questionable when NIE representatives consider culture (via beliefs, values and norms) as the main cause of good or bad economic performance. This is not to say that NIE exponents ignore factors like people's interests or desires. As the foregoing analysis illustrates, the problem with the considered NIE representatives is that they tend to assimilate interests and desires to culture, depriving them of their autonomy. Neoclassical economics and NIE seem not to consider appropriately the fact that human action consists of the interplay between interests, (cultural) beliefs and opportunities.¹⁷ No single determinant should be *ex ante* considered as crucial. Ascertaining which one in a specific case prevails is always an empirical question. In assessing the cultural influences on economic behavior we must resist both the assumption that culture makes no real difference as well as the assumption that through a privileged reference to culture we are able to explain the major contrasts in economic, political and social performance across the world (Senn 2001:11).

All this imply a methodological requirement for the researcher: for the analysis of dysfunctional economy on different levels of social aggregation (countries, firms, and families) a "balanced" conception of the actor is needed. This necessity is well formulated by Collier’s (2016:6) criticism against the advocates of a strict parsimony:¹⁸ „(o)nly by enlarging its account of behaviour can economics hope to provide an adequate account of severe social dysfunctions“. In this „enlarged“ model, behaviour is no longer entirely grounded in self-interested rationality; rather, „rationality only shapes decisions, once many beliefs have been uploaded from pre-rational network participation“ (ibid. 6). In other words, actors can be seen as rational utility-maximizers, but this orientation is conditional on beliefs which in turn are acquired through participation in cultural contexts and social networks „which are often pre-rational“ (ibid.: 6). Following a long tradition in social thought in which what we desire to do is distinguished from what we believe we ought to do, Collier’s does not subsumes norms into preferences but assigns to them a distinct role. On the other hand, he considers cultural beliefs embracing identities, narratives and norms as „a contributing factor“ among others. In the frame of a balanced conception of action the tension between desires (interests) and cultural beliefs should not be resolved at the expense of one of the two components,

at least not before empirical research produces enough evidence for this possibility.

IV) Conclusion

What conclusions can we draw from the previous analysis concerning different and partly reciprocally exclusive approaches to the problem of economic performance? A first general conclusion is that a non-reductivist conception of the social actor is needed. There can be no plausible explanations of economic performance when an actor's interests and his or her ability to make the „best“ use of given opportunities are either ignored or underestimated. However, it is also true that no explanation of economic performance is possible when an actor's cultural beliefs (values and norms) remain unsettled. Interests and beliefs, together with the existing opportunity, are necessary elements in reconstructing those mechanisms which on the micro-level of analysis generate and perpetuate social and economic phenomena on the macro level.

Neoclassical economists are surely right when they operate with a conscious and sometimes even critical actor, who rationally pursues interests, assessing constraints, and seizing opportunities. However, neoclassical economists are wrong when they conceive this actor as if she or he were moving in an institutionally and culturally free space. They are wrong when they see instrumental action as the only possible orientation for the actor.¹⁹ Focusing mainly on the actor's preferences, constraints and the (subjective) estimation of the expected utility, neoclassical economists usually do not ask about the origin of the preferences. To blind out this question, means to lose sight of cultural beliefs concerning what is considered a worthy pursuit.

The neoclassical definition of constraints is also questionable, insofar as it only takes specific kinds of limitations into account. The view that „(a)ctions are constrained by income, time, imperfect memory and calculating capacities, and other limited resources, and also by the opportunities available in the economy and elsewhere“ (Becker 1993:386) is too narrow. Neoclassical economists do not consider appropriately the fact that culture too – in the form of generalized as well as individually internalized beliefs, values and norms – constitutes important constraints for action. As we have seen, NIE representatives counter the reductionism of neoclassical economics with reference to a theoretical approach which puts culture at the center of attention. However, they cannot always escape the trap of culturalism.

Which mechanisms trigger and perpetuate bad equilibria based on generalized beliefs, and how can these equilibria be broken? Why and when do individuals conform to path-dependence, and under which conditions do they succeed in breaking these paths? Why do some groups have difficulties adopting the „culture of capitalism“, and under which circumstances are these groups able and prepared to abandon traditional ways of thinking and acting? These and other similar questions cannot be answered simply with exclusive reference to instrumental rationality *or* to culture. In this essay, a „balanced“ conception of action is the favored approach to escaping both the culture-blindness of Neoclassical thinking as well as the culturalism of some NIE-exponents. This means realizing that by pursuing own interests, actors move in a social and cultural space which provides them with opportunities, and at the same time places constraints on their actions. Further, it means realizing that these actors, in order to identify and to legitimize their interests, more or less explicitly make reference to ideas or beliefs which have their origin in specific cultural traditions. Finally, it also means realizing that there is a mutual conditioning relationship between interests, opportunities and beliefs.²⁰ No single determinant can *ex ante* be considered as crucial. Which one will ultimately prevail is a question that can be answered only by looking at empirical reality.

If we agree that individuals are not "trivial" creatures which smoothly conform to their social environment, we have no reason to consider culture as a natural force that renders individuals

powerless. On the other hand, we should avoid conceptions that portray individuals exclusively as profit-maximizers. Rationality does not necessarily have to be conceived of as „the relentless maximization of ‚self-interests‘ to the exclusion of other reasons for choice“ (Sen 2002:4). Even if in different ways, both the culturalistic as well as the rational ego-logic view abandon the important idea that human freedom means the possibility to choose autonomously between alternatives.

Notes:

- ¹ New-institution-economy (NIE) is the label under which economists find together sharing the common assumption that human action has to be considered as embedded in social institutions.
- ² In order to illustrate this point, I will refer to distinguished economists, sometimes quoting extensively. Most of the authors discussed in this essay are Nobel laureates: Gary S. Becker (1993), Douglass North (1993), Amartya Senn (1998), Edmund Phelps (2006), Oliver Williamson (2009), Robert Schiller (2013).
- ³ Although North (2010: 136-137) admits that the effects of religious beliefs on economic behavior are not clear, he attribute to the „beliefs structure“ of Christianity a special predisposition „to evolving in directions, that made it hospitable to economic growth“.
- ⁴ The question, to what extent collective beliefs can favor or hinder institutional and economic changes has also been raised by Avner Greif (1994:102) in his historical analysis, intended to illustrate the economic consequences of „collectivist“ und „individualist“ beliefs. As he writes, „cultural beliefs provide focal points and coordinate expectations, thereby influencing equilibrium section and society’s enforcement institutions“.
- ⁵ Pejovich underlines the fact that East-Block-States are not internally uniform, nevertheless he maintains that „All communities have their ‚mainstream‘ rules of the game...“ (ibid.: 348).
- ⁶ According to North (1994:14), „(t)he entire structure of the mental models is derived from the experiences of each individual - experiences that are specific to the local physical environment and socio-cultural linguistic environment“.
- ⁷ It is only in a later essay that Phelps (2013:195) admits: „There can be no doubt that new experience and new ideas can change a country’s culture“.
- ⁸ As Schiller (2018:972) puts it, narratives are cultural „scripts“ which persons adopt unconsciously as a role in situations of uncertainty or in ambiguous situations. Collier (2016: 8) stresses the fact that, as a specific type of beliefs, narratives are „acquired pre-rationally“, through participation in social networks. As he argues (Ibid. 8), „actors rationally maximize their utility subject to these beliefs, but the beliefs themselves are contaminated by these endowments of irrationality“.
- ⁹ Olson's second argument against culture as privilege concept is carried out with reference to „divided“ countries like China (Taiwan), Germany and Korea. In these cases Olson believes to be able to demonstrate that culture cannot be assumed as the variable which makes the difference: „Such great differences in economic performance in areas of very similar cultural characteristics could surely not be explained by differences in the marketable human capital of the population at issue“ (Olson, ibid.: 19).
- ¹⁰ As Becker (1993: 386) recognizes, „Forward-looking behavior, however, may still be rooted in the past, for the past can exert a long shadow on attitudes and values“. Becker does not develop this argument.

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- ¹¹ In this context reference to the mechanisms of „blocked exchange“ addressed by Beckert (2005) seems appropriate: „Blocked exchange refers to the prohibition or restriction of the monetary exchange of certain objects or services based on moral codes ... Blocked exchange prevents the market exchange of certain goods and services by keeping them outside the market realm ... Which transactions are blocked changes historically and differ between societies“ (Beckert *ibid.*:11). As examples for „blocked exchange“ Beckert refers *inter alia* to human trafficking, commerce with body parts, buying and selling of political decisions: „blocked exchange is not based on an economic rationale but rooted in social values“ (Beckert *ibid.*:12).
- ¹² This possibility is envisaged by Acemoglu & Robinson 2012.
- ¹³ Phelps writes: „Conspicuous inter-country differences in current-day participation, investment and so forth may stem from causal influence other than the neoclassic policy differences and the economic institutions just discussed: Perhaps differences in culture are an important influence on economic performance“ (Phelps 2005:10).
- ¹⁴ Cf. Sen (2001:8) „I would argue that maybe Japanese values have changed only a little, but the same ethical value have very different pay-offs and penalties in a substantially altered world“.
- ¹⁵ In an earlier web-version of the same essay Pejovich (2003: 15-16) refers to the interests of older people to continue in traditional paths: „Unlike young people, whose costs of adjusting to different informal rules are relatively low, members of the forty-something group feel that the time horizon is not long enough to allow them to adjust to the culture of individualism, self-efficiency and the nuclear family“.
- ¹⁶ This is not to say that neoclassical economics has nothing to say about the role of cultural values. The problem is that in neoclassical models, values are ultimately assimilated to the actor's utility (Akerlof and Yelling 1993). As Lindenberg (1983:451) puts it, „Conformity to moral rules is not a matter of expedient choice.“
- ¹⁷ Analytic sociologists like Elster (1989) and Hedström (2007) and others have illustrated different modalities of this interdependence. Interdependence, on the other hand, does not exclude the autonomy of these dimensions of action. With reference to social norms, Elster writes that „social norms provide an important kind of motivation for action that is irreducible to rationality or indeed to any other kind of optimizing mechanism“ (1989:15).
- ¹⁸ For a critical discussion of the concept of „parsimony“ by neoclassic economists see among others Hirsch, Michaels, Friedman (1987:320): “Economists pay a heavy price for the very simplicity and elegance of their models: empirical ignorance, misunderstanding, and, relatedly, unrealistic and bizarre policy recommendations“. However the following statement of Gary S. Becker (1993:385) shows eloquently that neoclassic economists are widening their horizon: „Along with others, I have tried to pry economists away from narrow assumptions about self-interests. Behavior is driven by a much richer set of values and preferences.“
- ¹⁹ The observation that instrumental rationality cannot explain why for individuals values like status or prestige (Frank 1985), uncertainty-reduction (Friedman, Hechter, Kanazawa: 1994) or justice by resources allocation (Jasso 1990; 1993) can sometimes be more important than material wealth-maximization sustains this view.
- ²⁰ Analytic sociologists like Elster (1989) and Hedström (2007) have illustrated different modalities of this interdependence. Interdependence, on the other hand, implies autonomy of the dimensions of action. Thus Elster (1989:15) with reference to social norms: „social norms provide an important kind of motivation for action that is irreducible to rationality or indeed to any other kind of optimizing mechanism.“

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