



Culture, Institutions, and Economic Performance*

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ABSTRACT

This paper focuses on the ability of two closely related phenomena, namely culture and institutions (especially the in-formal ones, such as codes of conduct, norms of behavior, and conventions), to impact economic performance. The main emphasis here is on the first of the two – the culture. The paper deals with the impact of the latter on economic activity and agents' behavior regarded from different viewpoints, including quantified and qualified ones. In addition, national and cultural differences of socioeconomic reforms are considered, as well as relations between culture and economic systems, culture and institutions, influence of cul-ture both on intra-firm and inter-firm relations, on the example of Russian corporations which use hybrid agreements and mechanisms of transaction management.

INTRODUCTION

From economic perspective, culture and institutions – especially considering the informal constraints such as “codes of conduct, norms of behavior, and conventions” – are related concepts. In fact, informal institutions are “*a part of heritage that we call culture*” (North, 1990, pp. 36, 37). In addition, the two are related in a sense that both contribute to economic performance. However, in this paper emphasis is made on culture and its ability to have an impact on the economic activity.

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The impact of culture on economic behavior regarded from the different positions, including quantified and qualified ones, is studied in (Yerznkyan, 2016a). National and cultural differences of socioeconomic reforms are considered, as well as relations between culture and economic systems, culture and institutions, influence of culture on inter-firm relations on the example of Russian corporations which use hybrid agreements and mechanisms of transaction management.

Examples of measuring institutions, as well as operations over institutions, meaning calculus of institutions, are given in (Makarov, 2003; Balcerzak and Pietrzak; 2016; Żelazny and Pietrucha, 2017). Issues of measuring the impact of institutions on the economic system with examples of direct and indirect institutional gauges are considered in (Shuaibu and Oladayo, 2016).

The outline of the paper is as follows. Section 2 describes culture and its relevance for economic activity. This section emphasizes the importance of culture in reforming the economy. Section 3 outlines the issues of incorporating culture in economic research. Section 4 shows the links between culture and economics systems. Section 5 deals with culture and institutions, accentuating the differences between reform characteristics and cultural specificity. Section 6 performs the impact of culture on inter-firm relations on the example of Russian corporations as well as its impact on intra-firm relations. Section 7 concludes.

1. CULTURE AND ITS RELEVANCE FOR ECONOMIC ACTION AND THINKING

Despite a long history of writers on the relationship between culture and economy, culture and economic theory, modern mainstream – neoclassical in essence – economics has been by and large silent on the topic of culture, on the ideas of the original institutionalists, evolutionary economists, social economists, and other followers of the other canon. However, recently the topic concerning the importance of culture for economic outcomes and the influence of culture on the economic process, are taking on renewed relevance. It is not surprising that most socially-oriented economists define economics as a cultural science. *“Its subject matter is the ever-changing world of economic phenomena that are bound to a very specific cultural context. Thus explaining economic phenomena requires acknowledging that economic actions and thinking are culturally conditioned, which in turn necessitates a procedure that takes seriously the efficacy of the cultural sphere and that does not reduce the cultural sphere to a mere economic residual”* (Goldschmidt, Remmele, 2005, p. 465).

The relevance of culture is of particular importance in reforming the economy. In (Martishin, 2015) it is shown that the strategy of reforms depends on the nature of the economic systems, assuming the measure of the gradual and radical development processes is based on the internal systems of genotypic regularities, which include the conservative and liberal lifestyles, their change and unity. To effectively reform Russia, the Russian genotype mutations, characterized by the excessive dominance of conservatory order, need to be eliminated. This can be done through an evolutionary reform strategy, assuming both the transformation of the old order and the gradual construction of genotypic economic models. Institutional trajectory of modernization should start with the “top” level of the existing features of economic systems and be concluded with the consideration of the general genotypic regularities of the global economic system, which does not deny the cultural and socio-economic features of the countries and regions. See also a paper (Arkhipov, Yerznkyan, Martishin, 2015), where the authors analyze evolutionary-institutional patterns and factors of economic growth and development on the example of a number of countries, which have demonstrated the “economic miracle”.

One of the first (perhaps, the very first and broad enough) definitions of culture is as follows: *“Culture or Civilization, taken in its wide ethnographic sense, is that complex whole which includes knowledge, belief, art, morals, law, custom, and any other capabilities and habits acquired by man as a member of society”* (Tylor, 1889, p. 1). Generally speaking, culture has multiple aspects or layers. For example, culture may be treated as tacit and explicit: *“Tacit culture is the cultural*

knowledge people don't put into words", while explicit culture "*consists of cultural categories that are coded in language*" (McCurdy et al., 2005, p. 8). In addition, economists have used culture with two different meanings: (1) as the social conventions and individual beliefs, as well as beliefs on the consequences of one's actions, where such beliefs are purposefully manipulated by earlier generations or by experimentation (e.g., Myerson, 1991; Greif, 1994), and (2) as the more primitive objects, such as individual values and preferences (e.g., Rabin, 1993; Akerlof, Kranton, 2000).

One can also distinguish between culture and its expressions as cultural values, beliefs, and attitudes. Culture, according to F. Gregory Hayden, is transcendent. Being "a collective systemic mental construct", it "contains a group's abstract ideas, ideals, and values", in addition, culture "is found in legends, mythology, supernatural visions, folklore, literature, elaborated superstitions, and sagas". As to values, they are "*cultural criteria or evaluative standards that allow us judge "what is ideal"*" (Hayden, 1988, pp. 415-416).

Relative to slow-to-change values, institution-specific beliefs and situation-specific attitudes are more malleable and "can adapt as necessary to align the demands of social participation with slower to evolve value criteria" (Adkisson, 2014, p. 92). Speaking of the influence of culture on the economic behavior, it should be underlined that behavior bears a relation not merely to actors, but to all other economic phenomena, such as, governance, which has "important influences on economic behavior", though they "are often ignored, discounted, or assumed away in empirical analyses" (see, e.g., Adkisson, McFerrin, 2014, p. 441).

2. INCORPORATING CULTURE IN ECONOMIC RESEARCH

One of the recent papers of Vitaly L. Tambovtsev (2015) is devoted to the critical analysis of today's mainstream approach to the inclusion of the factor of culture in economic research. According to him, national culture is treated as a reified entity in this framework, measured by societal values, and is persistently included as a "culture code" throughout different contexts.

However, there are a number of works contradicting to this idea and trying to suggest an alternative methodology for economic analysis of cultural phenomena. Let us selectively review some culture quantified – 'mainstream' as to Tambovtsev – works and then the 'alternative' – so called 'culture qualified' – ones.

Culture quantified approach. There is a good deal of definitions of culture. As to Geert Hofstede's shorthand definition, *culture is the collective programming of the mind that distinguishes the members of one group or category of people from others*. Being a collective phenomenon, culture can be connected to a verity of collectives, such as tribes or ethnic groups, nations, organizations, occupations, genders, generations, social classes and so on. For example, societal cultures reside (often unconsciously) in values, in the sense of *broad tendencies to prefer certain states of affairs over others*, while organizational cultures reside rather (visibly and consciously) in practices: the way people perceive what goes on within their organizational environment (Hofstede, 2011, p. 3).

Based on the statistical analysis and theoretical reasoning, Hofstede (1980; 2001) has proposed four cultural dimensions at first, with a fifth one being added later on. These five are:

- *power distance* as the extent to which the less powerful members of organizations and institutions accept and expect that power is distributed unequally;
- *uncertainty avoidance* as the extent to which a culture programs its members to feel either uncomfortable or comfortable in unstructured situations;
- *individualism* versus *collectivism* as the degree to which individuals are supposed to look after themselves or remain integrated into groups, usually around the family;
- *masculinity* versus *femininity* as the distribution of emotional roles between the genders;

- *long-term versus short-term orientation* as the extent to which a culture programs its members to accept delayed gratification of their material, social, and emotional needs (Hofstede, 2001, p. xix-xx).

Table 1 illustrates examples of the cultural differences between two neighboring nations in the Americas: United States and Mexico.

Table 1. Example of Cultural Differences between bordering nations: United States and Mexico

	Country	Mexico	USA
1	Power distance	With a greater power distance index value, Mexican society is more tolerant of inequality, in various forms, than the U.S. society.	In the absence of a greater power distance index value, U.S. society, compared to the Mexican society, is less tolerant of inequality, in various forms
2	Uncertainty avoidance	Having a higher uncertainty avoidance index, Mexican society is less tolerant of uncertainty.	Having a lower uncertainty avoidance index, U.S. society is more tolerant of uncertainty.
3	Individualism vs. collectivism	Mexican society tend to have a lower individualism (a higher collectivism) index value.	U.S. society is characterized by a higher individualism index value.
4	Masculinity vs. femininity	Mexico has a higher masculinity index value when compared to the US, although the difference is not as great as with the aforementioned dimensions.	U.S. masculinity (femininity) index value is comparatively lower (higher).
5	Long-term vs. short-term orientation	No long-term orientation value is available for Mexico.	The US are not a leader in this dimension, however when compared to Mexico they are more long term oriented (17 th place).

Source: derived from various tables in Hofstede, 2001. See also: Adkisson, 2014, p. 94.

Another line research has been undertaken by Trompenaars and Hampden-Turner (1998), which identify seven cultural dimensions (dilemmas):

- *universalism versus particularism (rules vs. relationships);*
- *individualism versus communitarism;*
- *affective versus neutral (degree of emotional expression);*
- *specific versus diffuse (private vs. public areas);*
- *achievement versus ascription (source of status);*
- *time orientation;*
- *relation to nature (internal vs. external orientation).*

In another example, let us compare two neighboring countries in Asia – China and India. The differences between the two are not only in culture, but also in terms of doing business and making foreign investments. Table 2 is an illustration of these differences, including culture, as well as the economic and political aspects.

Table 2. Example of the Cultural and Other Differences between China and India

<i>Country</i>	<i>China</i>	<i>India</i>
<i>Political and social differences</i>	Autocracy. Unitary state Leading role of one party Strong role of state ideology Mostly homogenous society Social class equality Relative success in fast poverty reduction	Federal democracy Multiparty system Pluralism Variety of languages, religions and cultures Caste system Absolute poverty country Disparity increases
<i>Economic policy</i>	Reforms began in 1979 Faster pace. Leader in FDI attractiveness Follows classical development route: Agriculture => Manufacturing => Services Export oriented manufacturing model Low cost manufacturing strategy Strong use of Diaspora capital Continuous flow of policies to build infrastructure, improve business climate Policies well planned and implemented Flexible labor laws. Merit-based system introduced Large size of Special Economic Zones Efficient tax holidays, export promotion, tax exemption on imported machinery, liberal entry and exit policies	Reforms began in 1991 Slower pace. Laggard in investor confidence Different to classical development route: Agriculture => Services (skipped the Manufacturing sector) Import substituting manufacturing model Skill intensive and services sector growth strategy Poor use of Diaspora capital Inconsistent policy in developing infrastructure No clear policy guidelines Rigid labor law Small size of Special Economic Zones Case by case basis in treatment of foreign investors. More place for corruption
<i>Cultural aspects</i>	Poor knowledge of English Relation-oriented managers	Good English language skills Project-oriented managers

Source: Vardanyan, 2011, p. 108.

In spite of many differences, there are some similarities between these two neighboring countries, as it relates to their economic development. They are as follows:

- in both countries the economic success is based on implementation of large-scale process of reforms, which are constantly under review by the government;
- both use a five-year plan as a framework of economic policy and designing of reforms;
- both employ economic instruments, e.g. attraction of Foreign Direct Investment (FDI) through fiscal incentive, to increase country competitiveness;
- both countries created free trade zones to accommodate foreign investments: Special Economic Zones in China and Export Processing Zones in India;
- the governments of both countries are willing to tackle the regional development problem and related issues to provide sustainable economic growth.

Nowadays, China and India keep each other in their eyesight and view each other as competition. One of the current distinctions between China as the 'factory of the world' and India as the 'world's back office' in international trade may be changing in the coming decade, since China is aiming to develop its service sectors, whereas India hopes to move towards skill-neutral mass manufacturing (Vardanyan, 2011, pp. 107-109).

With reference to the main advantages of the work of Trompenaars and Hampden-Turner (1998), it should be said "that they identify an alternative set of cultural dimensions, and explain their development and interpretation in very understandable language" (Adkisson, 2014, p. 96).

Intending to create a measure of American subculture, Joe Lieske proposed four properties for identifying ten regional subcultures. The properties are as follows:

- derivable from an explicit and replicable set of mathematical and statistical algorithms;
- reflects current cultural conditions;
- distinguishes sub-cultural differences down to the county level;
- based entirely on "nonpolitical" measures of American culture (Adkisson, 2014, p. 96).

Culture qualified approach. Such an alternative, in Tambovtsev's opinion, approach is based on the idea that each mass cultural practice should be analyzed on a "case-by-case" basis, comparing stakeholders' costs and benefits. In a sense, a culture qualified approach is based on the, so-called "inductive" method, as opposed to the widely known "deductive" method, cultivated by such authors as abovementioned Hofstede, Trompenaars, Hampden-Turner, and others. Such an inductive, in our terminology, approach to study the phenomena of culture is more productive, according to Tambovtsev, as the impact on the economic processes is assessed piece-by-piece, not in their totality. The "aggregate" cultural gauges, on the contrary, are arranged in a way that their influence on culture cannot be separated from the influence of formal institutions - starting from the values and ending with confidence.

3. CULTURE AND ECONOMIC SYSTEMS

G.B. Kleiner (2009) defines a system as a relatively independent part of the environment, stable in time and space, possessing both the properties of external integrity and internal diversity. A basic typology of economic systems includes a notion of system as: (i) *object* (a part of the external world, which exists outside a person. Examples of object systems are legal entities and individuals, organizations, regions, and republics); (ii) *process* (a cyclical pattern of a phenomenon's development. Process systems include higher education, science, art, innovations diffusion, inflation, and a country's economic growth); (iii) *project* (a sequence of steps aimed at achieving a specific goal within a specified time period and finally. Project systems include construction of a building, enterprise restructuring, elections of a CEO, and hosting of the 2014 Winter Olympics and so on); (iv) *environment* (a more or less homogenous matter filling space. Environment systems include the Internet, the stock market, the RF Postal Service, the national legal framework, an institution, and mass media).

Thus, objects, processes, projects, and environments are not only the most significant and widely researched part of economic phenomena and systems but, in fact, exhaust the variety of their types (Kleiner, 2009, pp. 9-10).

There are many studies on identifying the type of the existing and desired organizational culture, such as the well-known study of Charles Handy (1993).

Correlation between types of organizational culture and types of socioeconomic systems can be achieved by the comparison presented in Table 3.

Table 3

Table 3. System Types and Corresponding Types and Styles of Culture

<i>System</i>	<i>Culture</i>	<i>Type of culture</i>	<i>Style of culture</i>
Object		Zeus	Authoritarian
Process		Apollo	Bureaucratic
Project		Athenian	Project
Environment		Dionysius	Creating favorable conditions

Source: Handy, 1993; Kleiner, 2009, p.16.

Here, a Zeus culture (an authoritarian culture) enhances the properties of an organization, interpreted as an object system. Correspondingly, an Apollo culture (a bureaucratic culture) enhances the process properties of an organization, an Athenian culture (a project culture) – the properties of an organization as a project system, and, last but not least, a Dionysius culture (a culture oriented to creating favorable conditions for participants in activities) maximizes the environment priorities of an organization (Kleiner, 2009, p.16).

4. CULTURE AND INSTITUTIONS

Culture is one of the major factors explaining the notion of the widely divergent paths of historical change. “This divergence”, claims Douglass North, “is even perplexing in terms of standard neoclassical and international trade theory, which implies that over time economies, as they traded goods, services, and productive factors, would gradually converge”. But the puzzle is that we, in the whole, observe the divergence, not the convergence. Why is that? Because “*an overwhelming feature of the last ten millennia is that we have evolved into radically different religious, ethnic, cultural, political, and economic societies and the gap between rich and poor nations, between developed and underdeveloped nations, is wide today as ever was and perhaps a great deal wider than ever before*” (North, 1990, p. 6). To understand the differences between reform characteristics and cultural specificity, let us juxtapose Russia and China (see Table 4).

Table 4. Cultural and Institutional Differences and Market-Oriented Reform in Russia and China

<i>Country</i>	<i>Russia</i>	<i>China</i>
<i>Reform and cultural-institutional indicators</i>		
Level of development before reform	High	Low
Decline during reform	Significant	No decline
Growth rate after reform	Low	High
Sequence of reform	Politics first	Economy first
Pace of reform	Rapid	Gradual
Initiative of reform	Top-down	Middle-up
Spirit of reform	Shock therapy	Controlled transition
Nation’s propensity to revolution	Rather strong	Rather weak
Western advice (neo-liberal recipes)	Strong influence	No influence
Language	Synthetic	Analytic

Source: derived from tables in Yerznkyan, 2014, p. 67 and Rutland, 2009, p. 53.

From 1978 up to now, China has enjoyed average economic growth of roughly 10% a year, just like Japan has over the earlier three decades, i.e. from the mid-1950s to the mid-1970s. As to Russia, we have only reforms in the 1990s to compare with those of China to cover the spectrum of institutional change and cultural evolution, though “*we still are a long way from having any neat models of cultural evolution*” (North, 1990, p. 44). However, it is rather unquestionable that cultural traits have tenacious survival ability and that most cultural changes are incremental, not decremental, and as such they essentially matter.

5. THE IMPACT OF CULTURE ON INTER-FIRM AND INTRA-FIRM RELATIONS

It is appropriate to consider the impact of culture on inter-firm relations. In (Popov, Simonova, 2015), this impact is studied on the example of Russian corporations which use hybrid agreements and mechanisms of transaction management. The authors empirically determine the dependency of the impact of the specificity of resources on the transactions of hybrid organizations. However, for the purpose of the present paper, it is of special interest the authors' outline of the specific cultural characters of the organizations of inter-firm cooperation in the Russian industrial market and some of Russian-specific cultural factors applying to these organizations revealed by them. Here are these factors:

- under the conditions of instability, personal relationships and past experiences of mutual obligations, which are factors in the formation of trust, are not able to fully mitigate the risks associated with specific assets. As a result, as asset specificity grows, trust in the partner and confidence in the implementation of agreements is reduced;
- the weak legal institutions underpinning the Russian economy were found to exert a strong influence on the parameters of informal ties of the corporations' inter-firm cooperation;
- greater significance is accorded to the mechanisms impacting the partner and the control of the implementation of the contract, forming an alternative to trust;
- over the past decade, the consolidation of management functions began to implement control functions without, as a general rule, also unifying the assets of various actors, i.e. on the basis of legal independence (Popov, Simonova, 2015, p. 50-51).

The theoretical and practical analysis of transactions of hybrid organizations, concluded Evgeny Popov and Victoria Simonova, demonstrates the possibility of a theoretical description of contemporary inter-firm interactions and a determination of the specific manifestations of transactional relations under the contemporary conditions of Russian industrial corporations. An example of impact of (speech) culture on intra-firm relations is presented in (Yerznkyan, Lignovskaya, 2014), where the features of intra-firm managerial transactions, through a prism of influence of speech culture (verbal, as well as non-verbal), are considered. It is shown that a skillful use of speech culture can be a factor in increasing the level of managerial competencies and, consequently, the efficiency of managerial transactions. Possibilities of extraction of a speech rent, problems of language sign, as well as the other issues concerning the impact of the managerial transactions within firm on efficiency, are discussed. Another example of (organizational) culture, which matters for minimizing working capital being extremely important for any company that is willing to not only continue its existence, but more importantly, for a company willing to grow, is given in (Gassner, 2011). The conclusion of the author is as follows: “*while many organizations might appear profitable on paper, quite often they find themselves in a position where they are unable to pay their short-term debts as they come due, and, as a result, they are forced into bankruptcy. In order for companies to be efficient they need to strive towards minimizing their working capital, and if possible (depending on the industry and type of business) move towards negative working capital. However, there is a fine line between negative working capital resulting from highly efficient operations and negative working capital leading to bankruptcy. A part of minimizing working capital is determining the ‘minimum’ that ‘fits’ the company and increases its efficiencies*” (Gassner, 2011, p. 112).

CONCLUSION

From the perspective of institutional approach, culture, according to Tambovtsev (2015), is a set of practices that reflect both adherence to and violation of the norms, as well as the discretionary decisions taken in specific situations.

With regard to the mainstream economists, they have recently begun to pay a greater attention to cultural influences on economic activity. One of the answers to the evident question “why”, is that *culture matters*. It matters today, it matters tomorrow - it can positively or negatively shape the future of organizations. It matters because of its ability to influence economic activity. Evermore, it matters because of its deeper and more holistic ability to construct the economic reality as such. There are a lot of dimensions for culturally predetermined reality, including morality and related issues. “A culture that no longer has a point of relevance in God loses its soul and loses its way, becoming a culture of death. Detached from their Christian origins, these models are often inspired by an approach to life marked by secularism and practical atheism and by patterns of radical individualism” (Pope, 2001).

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