

Diversity and Pluralism: An Economist's View

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- **Second Conference “Qualitative diversity research: Looking ahead”**, 19-20 September 2006, K.U.Leuven, Leuven, Belgium. Contact person: Maddy Janssens, maddy.janssens@econ.kuleuven.ac.be, and Patrizia Zanoni, patrizia.zanoni@kuleuven.ac.be
- **Third Conference “Diversity in cities: Visible and invisible walls”**, 11-12 September 2007, UCL, London, UK. Contact person: Valeria Papponetti, valeria.papponetti@feem.it
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This batch of papers has been presented at the first EURODIV Conference “Understanding diversity: Mapping and Measuring”.

Diversity and Pluralism: An Economist's View

Summary

The problems about diversity concern various themes. We will show that the economic theory can contribute by itself to the debate in progress. It could seem paradoxical, but what is called the “dismal science” can serve to attenuate some pessimistic attitudes, putting in prominence a perspective for humanity which is desired. To introduce such contribution, we have examined some essential characteristics of neoclassic theory, regarding the typical features of the individual which it assumes and the principle of “rationality”. Our analysis emphasizes the importance of the economy of market which prevails on other economic systems and makes possible the realization of a “culturally sustainable development”. It also examines the economic benefits of diversity both on the function production and the possibility to have a dynamic demand of goods. The difference between integration and homogenization will be treated and also the importance of international commerce and direct investments.

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1. Introduction

In these last years, the problems of the coexistence of different cultures have been considered very important. Studios of the whole world, belonging to various disciplines direct their attention on them. Wide space is given to them also in the political circle, mass media and television.

These problems, that have always existed, are certainly whetted because of propagating of globalizations phenomenon and of increasing migratory flows in the world.

Questions about diversity and cultural pluralism concern various themes, such as ethics, religion, sociology, psychology, anthropology and politics. Therefore, for many authors, the economist necessarily must go out of the circle of his own studies to develop an interdisciplinary investigation.

We will show how the economic theory can contribute by itself to the debate in progress. It could seem a paradox, but what it's called "dismal science" can serve to attenuate some pessimistic attitudes, putting in prominence a positive and desired perspective for humanity.

To introduce such a contribution, we will examine some essential characteristics of the neoclassic theory. The purpose is to consider the problems of the cultural and ethnic diversity in their real configuration, under the economic aspect.

The plan of the paper is as follows. Section 2 analyses diversity from Neoclassical theory point of view. The interrelations among the integration of different ethnic groups, the productivity of production factors and the size of market economy systems are examined in Section 3. Where the difference between integration and homogenization are also indicated with regard to the Culturally sustainable development. Section 4 faces the relation between diversity and international commerce. At last globalization and costs of diversity are discussed in section 5.

2. Neoclassical theory and diversity

The neoclassical theory put at the centre of its analysis the behaviour of the single individual, without making distinction between culture, race or religion. The essential characteristic that the individual has to have is about the knowledge and the information, together with the aspiration to

improve his economic conditions, satisfy desires and realize objectives, through choices which are driven by the criterion of “rationality”. This precise statement has the value of an axiom, since it concerns what differs men from all other living beings.

The economic theory individualizes only one economic system which, as history has shown, can allow the coexistence and interrelation, for the attainment of a commune objective, between single individuals also belonging to different cultures. Such a system is the economy of market, which, in its ideal conception, foresees the possibility to eliminate the exploitation of one man from another. This is very important because, if such a possibility exists a notable contrast would be inevitable, and it would be source of attritions and negative aspects, especially among ethnic groups with different cultures.

If we look at the past, such negative effects are occurred because of differences about knowledge and information and they have been increased by the concentration of the power in the hands of people belonging to privileged classes. Also for populations with the same culture, strong contrasts, serious social tensions and the phenomenon of the exploitation prevailed. But these situations of attrition get worse, when different ethnic group come into contact. Besides the aforesaid differences of knowledge and information, there are diverse cultural and racial characteristics.

The economy of market has allowed us not only the elimination of privileges guaranteed to some social classes against others. But exalting the positive aspects of the cultural pluralism, it has also permitted the integration of groups with different ethnic characteristics in the same economic reality. At this point of our discussion, perhaps, it is necessary to underline other fundamental characteristics of the economy of market, that allow us to reach the aforesaid results. It's important to remember the incidence of competition which in such system makes its effects felt on the choices of consumers and entrepreneurs.

In the economy of market, consumers have full liberty of choice. They can influence the productive activity on the base of their preferences, in such a way that, in the ideal theoretical model, they can be considered the true holders of economic power. Entrepreneurs, under the push of competition,

are stimulated to minimize costs of production and increase more and more productive efficiency. At the same time, they introduce innovations, both in productive technology and in the creation of products, with the purpose of respecting the consumer's preferences.

In a market economy, the integration of heterogeneous groups is possible, since it can have positive effects on the creation of a dynamic and more varied demand of goods.

This is an aspect not to be neglect, since it constitutes a fundamental factor for the development of an economy of market; its lack represents one of the greatest dangers, because it is a source of economic stagnation and crisis.

3. Integration, productivity and size of Economic market systems

Integration has also a highly positive value regarding the productive aspect. The presence of diverse individual ability coming from different ethnic groups can be compared to the availability of different productive factors for entrepreneurs. Such factors have a complementary validity in production and they allow us an increased productivity and a greater ability for creating innovation.

About this concept, Lu Hong e Scott Page (1995)¹ present two important results. They say that a group of individuals with different intellectual abilities can find optimal solutions for very difficult problems. Besides, they affirm that, under certain conditions, a group of people with limited ability can get better results than another group of individuals who have greater ability. Such a result is based on the intuition that the probability that an individual effects better choices than another depends mainly on the different perspective from which he studies the choices to realize.

Such a reality has been underlined by many economists. Recently, it has also been put in prominence by Alesina, Spolaore e Wacziarg (2000)². They use a function of production with more variety of inputs, already introduced by Dixit-Stiglitz, for showing that this variety increases total output. Such a function can be considered in simplified form³. For example, if we consider a community with K

¹ Lu Hong and Scott E. Page, (1995), *Diversity and Optimality*, Santa Fe Institute, Working Paper 98, 08-077.

² Alberto Alesina, Enrico Spolaore, and Romain Wacziarg, (2000), *Economic Integration and Political Disintegration*, American Economic Review, 90 (5), pp. 1276-96.

³ Alesina Alberto and Eliana La Ferrara, *Ethnic Diversity and Economic Performance*, Journal of Economic Literature, 43 (3), 766-767.

different types of individuals, for a total population of N people and if every group of such individuals has the same size $s=N/K$, the level of production of this community is given by: $Y= N f(x,K)$, where x is the fixed amount of input, say labour, common to every group and with equal productivity. We assume that $f_x > 0$ e $f_{xx} < 0$. As the existence of diverse ethnic groups allow the availability of different production factors, which is a positive element, then we assume $f_K > 0$ e $f_{KK} < 0$. Therefore per capita income is an increasing function with respect to the number of different existing groups in the population. The aforesaid formulation constitutes the simplest possible way to put in prominence the benefits for production created by the variety of productive factors. The complementarity among different abilities of diverse groups and the factor x is indicated by $f_{xK} > 0$. This determines that an augmentation of diversity, with a greater number of groups (K), which have different ethnic characteristic, increases productivity of the factor (x) common to all existent groups in the community.

From this simple model, it is possible to draw an immediate consequence: if the complementarity of K in respect of x is positive and sufficiently large, the higher is the level of per capita income the ampler is the utilization of factor x . Therefore, it is necessary an increasing of K (the number of groups with different ability) in order to maintain an elevated productivity of factor x .

This complementarity increases the benefits of diversity and makes possible the integration of a greater number of different groups. In fact, as the individual product grows, productivity of common factor x is maintained or increased by a greater diversity. Therefore the consequential benefits from more ethnic heterogeneity are increasing when the level of per capita product is growing.

This result is empirically verifiable. The advantages of diversity regarding the productive ability are more remarkable in the most advanced and complex societies.

In fact, in the countries with an high level of income, there is certainly an economy of market which goes well and is endowed with the necessary institutions. In it every individual is in condition to operate on the free market to realize his own welfare objectives. On the other hand, a developed country with a high level of income presents a very complex economy, particularly about

specializations of operators and variety of products to offer to consumers. These conditions are optimal for the integration in such an economy of an increasing number of groups of individuals with different ethnic and cultural characteristics. They will allow a variety of productive abilities and contemporarily a dynamic and varied demand of goods to be made available for such an economy, as we have already noted.

These considerations allow us to explain the “dilemma”, which some economists have observed when looking at the economy of the United States and the situation of countries with a lower level of income. This “dilemma” derives from the actual reality of the United States. This country is an economically successful melting pot. Notwithstanding the large different ethnic groups it reached an elevated rate of growth of productivity and realized a constant creation of innovations in production and also in arts and cultural activity. In other countries, with a lower level of development, the presence of heterogeneous ethnic groups gives limited advantages, from the economic point of view, as the common factor productivity is not so high. The increase of number of different ethnic groups could make the situation of this country worse as regard the cost of cultural pluralism and ethnic diversity, about which we can give a short account at the end this paper.

This particular aspect is approved not only by the dominant neoclassical theory, which exclusively analyzes the interrelations among economic operators, without considering the role of institutions, but it is also accepted by a different school of economists called “Neo Institutionalism”. This school, instead, attributes greater importance to the institutional system.

On this matter an ample concordance can be noticed between the two schools. It is enough to examine the article of Andreas Kyriacou⁴. He introduces a review of contributions of Institutional economist, which deepens the links among ethnic differences and institutions, within the theory of rational choices. Such economists openly underline the necessity that in the economic system, besides the institutions directed to reduce the social and ethnic conflicts created by diversity, it is necessary to have an ample and developed market economy, in which the interrelations and the

⁴ Andreas Kyriacou, (2005), *Rationality Ethnicity and Institutions: A Survey of Issues and Results*, Journal of Economic Surveys, 19 (1), 23-42.

exchanges are realized in a formal way, independently from the ethnic characteristics of contracting parties.

In other economic systems, different from the economy of market, there are many examples of great contrasts and processes of exploitation of man, as well as of prevalence of a culture on the other.

It is enough to think about the most evident example regarding the period of the slavery in the United States of America, when millions and millions of people were eradicated from their place of origin, to use their workforce in another country, without any possibility to improve their conditions. Only survival, but not always, was assured to such people, as they were being considered simple tools to be maintained in condition to produce.

Such situation was interrupted after the war of Secession, when slavery was abolished. Later, in the United States, a process of integration began, not only for the ex black slaves and their descendants, but also of many other immigrants, belonging to different ethnic groups.

The process of integration has been gradual but continuous and was achieved because in the United States of America the economy of market was in force. In this economic system the real possibility to undertake and to insert himself in the structure of economic reality, exists for every single man. This process of integration has followed a tortuous and tormented path, but the correct direction has prevailed.

Another example concerns the shattering in different States of the Soviet empire. This points out that an economic system where there isn't the market economy, but there is the planned economy, integration is impossible. In the Soviet empire the integration of different ethnic groups wasn't realized, despite a period of more than seventy years passed.

Also Yugoslavia after the death of Tito was split into diverse States. And in this case there were disastrous wars and much destruction.

At this point, we would not like the reader to think we are using the word integration as synonym of homogenization. A notable difference exists between these two phenomena. It is not considered by those who use the term integration but suggest politics and external interventions which instead lead

to homogenization. The latter process would be in contrast with one of the fundamental bases of modern economic theory, which foresees the coexistence of different individuals, such as consumers, entrepreneurs and dependent workers, with diverse preferences, manifold aspirations, different ability and incentives to produce .

It is more probable that such a condition is present in a process of integration, when people with different cultures but with suitable level of knowledge come into close contact and operate in the same environment of market economy, maintaining their own cultural characteristics. With homogenization of the behaviours of different coexistent ethnic groups, in the same economic system, advantages of integration are lost, as we have already underlined, both in economic terms and under social aspect.

The market economy, therefore, can be considered as the only economic system which can realize, through the integration of different ethnic groups, “a culturally sustainable development”.

Such an aspect is of great importance, since many other social disciplines currently consider the maintenance of cultural pluralism very necessary, because in every culture there are values which we must not lose.

4. Diversity and international commerce

Now we must return to the aforesaid affirmation about the importance of country level of economic development and the degree of complexity of its economy to allow a more and more elevated possibility of integration regarding different ethnic groups. Now it is necessary to add some qualifications concerning the international commerce.

We have to remember the historical role of international commerce. The economic theory has given a particularly elevated relevance to it. In fact, we must consider the Hecksher-Ohlin model, formalized by Samuelson, in which international exchange goes toward the equalization of labour remunerations, without any movement of workers from one country to another. It could be objected that integration among different ethnic groups is possible not only in a great economic system, since these groups can use the alternative granted by international commerce. Its importance however

depends on the intensity and the structure of exchanges, which it allows. In reality, the commercial flows at international level are hindered by national frontiers, even if free exchange is in force without explicit customs barriers⁵. If we hypothesize the existence of rigid commercial restrictions, the size of a country, with the aforesaid economic characteristics, remains the only important factor for the integration of different cultures.

It is necessary, however, to note that the existing different ethnic groups in a country can help its international commerce. For instance, a certain ethnic minority in the country A can constitute a link with the country B, where this ethnic group constitutes the majority, then facilitating the exchanges between A and B.

This phenomenon is not marginal; we have many empirical researches and also theoretical elaborations which show the importance of aforesaid link both for international exchanges and a greater economic integration among different cultures⁶.

In general, however, the alternative created by international commerce appears less effective than the integration of different ethnic groups realized in the same economic system. The international commerce can hardly bring that level of integration we desire, both because it concerns relatively few products and because it constitutes a rather small instrument through which the knowledge and the productive abilities can be extended.

In the same optics, we can also consider the process of integration and diffusion of knowledge and information which occurs through the direct investments of countries economically developed in others with an inferior economic level and different characteristics under the ethnic and cultural aspect. In fact, also this phenomenon which economists have treated, especially in reference to the role of the multinational enterprises, has not obtained results of great relevance for a sustainable development in cultural and economic terms, although it operates in the correct direction.

⁵ Su questo tema si veda Alberto Alesina Robert J. Barro and Silvana Teneyro, "Optimal Currency Areas", in NBER Macroeconomics Annual 2002. Mark Gertler and Kenneth Rogoff, eds. Cambridge: MIT Press, 301-55.

⁶ Samuel P. Huntington (1998), *The Clash of Civilizations and the Remaking of the World Order*, New York: Simon and Schuster; James E. Rauch and A. Casella, (2003), *Overcoming Informational Barriers to International Resource Allocation: Prices and Ties*; Economic Journal, 113 (484), 21-42.

5. Globalization and costs of diversity

For the future, we must think about globalization, which allows, increasingly, the diffusion of knowledge and information, thanks to the technological progress in the field of telematics. If this phenomenon could completely realize its positive aspects, together with the reduction of its negative reflexes (both constitute a theme currently very debated), the international commerce will be able to become the best way for the integration of different cultures. It would reduce the costs of diversity, deriving from coexistence between different ethnic groups, since the migratory flows would decrease, until they become null. Regarding these costs of diversity, till now we have not made any reference to them and we can give only a short account.

In reality, our relation has been devoted entirely to identifying the advantages of ethnic diversity and pluralism of cultures, drawing from principles of economic theory and observing the reality of economically advanced countries, in which such principles find their effective realization.

We are conscious of potential costs of diversity. They are fairly evident under ethnic and political aspect: difficulty in the communication among people with different languages, cultures and preferences, racism and prejudices. The latter two can determine harmful politics for the whole community.

The economists have also analyzed such costs and they tried to identify the best level of heterogeneity, finding the optimal value of a trade-off between costs and productive advantages. This trade-off emerges from numerous recent studies. Some of these put the accent on the organizational aspect. For a review of these studies, it is possible to consult the articles by Susan Jackson and Marian Ruderman and Orlando R. Kochan and Amy McMillan-Capehart⁷.

The economic researchers, still regarding the analysis of costs, have put in prominence a particular type of goods and services, which they call public goods, offered by State to the whole community.

They affirm that the sharing of the same public goods by different ethnic groups implicates contacts

⁷ Susan E Jackson and Marian N. Ruderman (1996), *Diversity in Work Teams: Research Paradigms for a Changing Workplace*, Washington, D.C.: American Psychological Association; Orlando Richard, Thomas Kochan and Amy McMillan-Capehart (2002), *The impact of Visible Diversity on Organizational Effectiveness: Disclosing the Contents in Pandora's Black Box*, Journal of Business and Management, 8 (3), 265-92.

among people not disciplined by the market, which are source of negative utility. Such an aspect is studied in depth in the article by Alberto Alesina and Eliana La Ferrara⁸.

A different interpretation derives from consideration of different types of public goods in a context where every public good is selected on the basis of preferences of the "Median voter". In this way, the ampler the number of existing ethnic groups, the greater the average distance between every group and "Median Voter" on basis of whose preferences the State chooses public goods. Economists, therefore, have put in prominence the existence of a negative relationship between utility of their consumption and the number of existing different ethnic groups.

This problem cannot be resolved by the market, since it cannot furnish such public goods. The development of economy of market and its institutions can reduce in meaningful way the other costs mentioned above. While as regards the optimal offer of public goods, we can imagine the negative influence of diversity can be weakened in the long period and be compensated by advantages, which the difference among ethnic groups allows us in terms of quality and productivity of private sector goods.

Concluding remarks

To conclude, we want to underline that the problem of ethnic diversity has become remarkable for Europe. It has had a greater ethnic homogeneity than United States, but the widening of the European Union and the increasing immigration from Africa and from other nearby areas will determine that the member countries of Europe will become less and less homogeneous and therefore also for them, in the near future, there will be the problem of facing the challenge set by cultural and ethnic diversity.

⁸ Alberto Alesina and Eliana La Ferrara, (2000), *Partecipazione in Heterogeneous Communities*, Quarterly Journal of Economics, 115 (3), 847-904.

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