

# **Multiculturalism and Economic Growth**

**by**

**Gerald W. Scully**

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**National Center for Policy Analysis  
12655 North Central Expressway  
Suite 720  
Dallas, Texas 75243  
(214) 386-6272**

# Executive Summary

Multiculturalism is in vogue today among academicians, politicians and the media. But anthropologists identify cultural diversity as a universal source of social conflict and often as a barrier to economic progress as well as personal freedom.

Culture includes learned patterns of behavior, socially acquired traditions, repetitive ways of thinking and acting, attitudes, values and morals. Culture standardizes relationships by allowing people to make reasonably confident assumptions about the reactions of those with whom they interact. There are many dimensions of culture, but race, religion, ethnicity and language are the principal sources of diversity. When societies are multicultural, the ethnocentric differences of race, religion, ethnicity and language often lead to enmity. Even if different groups live together peacefully, the lack of a common language and common norms reduces cooperation and increases the cost of transacting.

Cultural relativism has made the study of the role of culture in human progress controversial. But there is little disagreement that intergroup enmity is widespread in culturally heterogeneous societies. This study shows that cultural diversity and a lack of economic freedom go hand in hand.

Free markets, private property, rule of law and eventually representative democracy and universal suffrage arose in culturally homogeneous Western societies where *all* members of society had equal rights to compete in the marketplace. On the other hand, culturally heterogeneous societies are less likely to adopt the institutions of liberty. Since control of economic resources is essential to political control, dominant cultural groups structure economic institutions to serve their self-interest. And when private property and economic rights are allocated along cultural lines, economic inefficiency is inevitable and societies are less prosperous.

For all its problems, the West has managed cultural conflict better than the rest of the world because it has free economic, civil and political institutions. Partly, the tension associated with the absorption of different cultures through immigration has been diffused because our institutions protect individual freedom. Partly, tension has been reduced by efforts to homogenize immigrants into the dominant culture.

Despite this success, we are moving away from the notion of *individual* freedom to that of *group* rights in the United States. Increasingly, ours is a country where one's standing before the law is a matter of group membership. Specific rights and entitlements arise solely because of membership in a group.

Outside of the West, cultural heterogeneity has caused social instability and retarded economic progress. Furthermore, a lack of personal freedom is correlated with the degree of cultural heterogeneity in many non-Western societies. More and more, scholars and Western politicians are recognizing that the key to economic transformation of the Third World is its move toward freer institutions and that cultural heterogeneity is the major barrier to such transformation.

## Introduction: Freedom and Economic Growth

Five or six centuries ago, most of mankind had a similar living standard. Western Europe was not better off than other areas around the world. Great kingdoms existed in Asia and to a lesser extent in Africa. For centuries, the Chinese were more technologically advanced than the Europeans. When Britain began colonizing India in the mid-18th century, the Indian subcontinent was not significantly less developed than the British Isles.<sup>1</sup>

Today, however, the disparities in living standards are remarkable and growing worse. Among the poorest nations, per capita consumption is a tiny fraction of that of the West.

- For the entire Third World, the growth in per capita real domestic product was positive but small throughout the 1980s; in the early 1990s, Third World economic growth was negative.
- Life expectancy in the poor nations is a third of ours.
- Babies die 30 times more frequently.
- And electrification, a necessity for applying mechanical advantage and more advanced technologies to production, is at the stage ours had reached a hundred years ago.

Why is the West so rich and the rest of the world so poor? Economists have struggled with this question since the end of World War II. Beginning with Robert Solow's 1956 paper on the neoclassical theory of economic growth, we have focused on the rate of capital formation and technological change as sources of the engine of growth.<sup>2</sup> Later, human capital (schooling and job training) was added as an important factor.

Neoclassical economists take the institutional framework of a society as irrelevant to the theory. By implication, if you plunk down a unit of capital in Zaire or in Cuba, it should have the same incremental effect on output as in Hong Kong or Costa Rica. But experience shows that it does not. A major contributor to the difference in economic outcomes is in the difference in the institutions each nation chooses.

Generally, we distinguish between economic, civil and political liberty. Economic liberty means the right to private property, freedom of contract and a free market allocation of all goods and services, including external trade, and of all productive inputs.<sup>3</sup>

Civil liberty means the protection of individual rights. In the broadest sense, it means the rule of law. In a narrower sense, civil liberty is defined in the Constitution and the Bill of Rights.<sup>4</sup>

Political liberty means the right of the people to choose who rules them and gets to use the coercive power of the state. While "democracy" is the common usage, in fact there are no real democracies. The United States has representative government, universal suffrage and majority rule.

*"The disparities in living standards among countries are remarkable and growing worse."*

## Measuring Political and Civil Liberty

The most comprehensive measures of political and civil liberty available today are those constructed by Freedom House.<sup>5</sup> Since 1973, it has constructed annual indexes of political and civil liberty for virtually all nations.

**Political Liberty.** The measure of political liberty is from 1 (the highest degree of liberty) to 7 (the lowest), based on rankings of several subjective criteria. The criteria are the meaningfulness of elections for the executive and legislature (as an expression of the will of the people); election laws and campaigning opportunities; voting power of the electorate (electoral vote-weighting such as gerrymandering a congressional district to give racial preferences); political competition (multiple political parties); evidence of political power shifting through elections; significant opposition voting; freedom from external and military control of domestic politics; minority self-determination or pluralism; decentralization of political power; and the efforts of politicians to reach consensus on national issues.

**Civil Liberty.** The measure of civil liberty, ranked on a similar scale, is based on rankings of such criteria as freedom of the press; freedom from political censorship; freedom of speech, assembly and peaceful demonstration; freedom to organize for political purposes; equal protection under the law; freedom from arbitrary property searches and seizures; an independent judiciary; freedom from arbitrary imprisonment; freedom from government terror and abuse; free trade unions and worker associations; free business and professional associations; and freedom of religion. Other criteria include protection of social rights (including freedom of property, internal and external travel, choice of residence, marriage and family); protection of socioeconomic rights (including freedom from dependency on landlords, bosses, union leaders or bureaucrats); and freedom from both gross socioeconomic inequality and government indifference or corruption.

**Ranking Countries.** I have averaged the values of the Freedom House measures of political and civil rights by country from 1973 to 1986. Because this period predates the collapse of the Soviet Union and the revolutions in Eastern Europe, the numbers I derived understate the degree of political transformation now under way in the former socialist bloc.<sup>6</sup>

Broadly speaking, about 30 percent of the nations in the world have free political and legal institutions, about 35 percent have no freedoms and the remainder are partly free. Dictatorship is the most common form of government in the world. About three-quarters of all countries are dictatorships or dominant-party states.<sup>7</sup> Multiparty political systems in which there is credible political competition are found mainly in capitalist nations characterized by private property, free enterprise and free markets. About 40 percent of the

*“About 30 percent of nations have free political and legal institutions, about 35 percent have no freedoms and the remainder are partly free.”*

capitalist countries have multiparty political systems. The others are dictatorships or dominant-party states in which the government dominates the economy.

## The Link Between Liberty and Economic Growth

What empirical evidence exists on the relationship between freedom and economic growth?

**Early Studies.** Most studies have focused on the link between political institutions and economic growth. Of six early studies, five found that the economies of authoritarian regimes grew faster than those of democratic regimes. Probably the best known was the study by Irma Adelman and Cynthia Taft Morris, which influenced World Bank attitudes, lending and policy toward the less-developed world.<sup>8</sup> Unfortunately, all the early studies suffer from fundamental research design flaws. The most important flaws are the crudity of the measures of political freedom and the transformation of national income account data in local currency into U.S. dollar equivalents using official exchange rates. In non-Western countries, these rates often bear little or no relationship to the purchasing power of the currency.

The more modern studies use data supplied by Robert Summers and Alan Heston, who adjust national income accounts for purchasing power parity.<sup>9</sup> Also, modern studies use better measures of political freedom. Of the nine broad-based studies with which I am familiar, six found that the growth rate was higher under democratic political regimes, one found growth higher under authoritarian regimes and two found no difference. However, focusing exclusively on the effect of the political system is too narrow. A better approach is to consider the effects of measures of liberty.

**Scully Study.** My 1988 study that linked economic growth and economic efficiency to measures of economic, civil (legal) and political freedom found the effect of institutional choice to be not only significant but of a large order of magnitude.<sup>10</sup> [See Figure I.]

- From 1960-80, the growth rate of real domestic product per capita for the average nation with a high degree of economic, civil and political liberty was 2.7 percent per year.
- During that period, the average nation with proscribed individual rights grew at 0.9 percent per year.

**The Importance of Institutional Choice.** Both theory and the empirical evidence on the link between institutions and economic growth point to several inescapable conclusions:

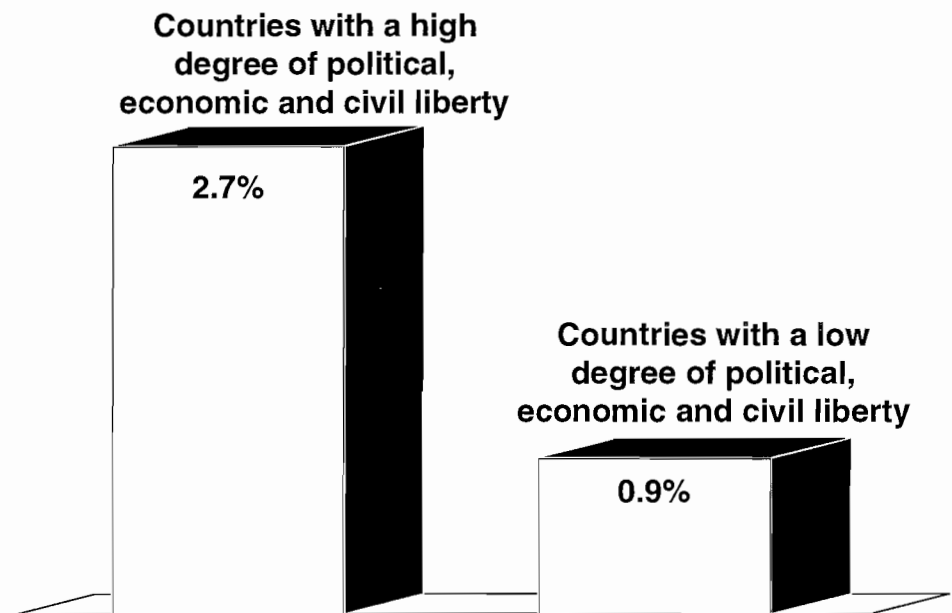
*"The degree of economic, civil and political freedom significantly affects economic growth."*

"The growth rate for countries with a high degree of liberty was 2.7 percent per year, compared to 0.9 percent for those with a low degree."

FIGURE I

## Economic Growth Rates

(1960-80)



Source: Gerald W. Scully, "The Institutional Framework and Economic Development," *Journal of Political Economy*, 86, June 1988.

- Economic freedom and rule of law are fundamental for high levels of economic growth.
- Security of property, freedom of contract and free market exchange promote capital formation and, hence, economic growth.
- A legal system based on law rather than men's whims stabilizes the rules under which resources are allocated.
- Without institutional protections of individual freedom, transforming poor nations into rich nations is virtually impossible.

There is less agreement about the link between political freedom and economic growth. Historical evidence suggests that the economic transformation of the West was not accompanied by political freedom as we now know it. By political liberty we mean representative government, universal suffrage and majority rule — 20th-century inventions.<sup>11</sup> Moreover, some would assert that our modern political institutions have led to a tremendous growth in the size of the state, which is a threat to liberty, and to a substitution of the allocation of scarce resources in the political market for allocation in a free market. The political allocation of resources is less efficient and leads to lower economic growth.

## Multiculturalism and Institutional Choice

Multiculturalism is in vogue today among academicians, politicians and the media. Perhaps we as a society aspire to pluralism. But anthropologists identify cultural diversity as a universal source of social conflict and often as a barrier to economic progress, as well as to personal freedom.<sup>12</sup>

**The Growth of Freedom: England.** A fair reading of history reveals that economic, civil and political freedom arose in a homogeneous culture — England. Common law is very old, probably arising in Ireland in the fifth century. When the Normans conquered England in 1066 they allowed common law as the law of the land, since they had no alternative legal system. Common law was institutionalized between 1154 and 1307, under the kings from Henry II to Edward I. Thus, judge-made rule of law was a feature of the English system long before the Industrial Revolution.

*“Economic, civil and political freedom arose in a homogeneous culture — England.”*

Private property evolved in England as the monarchy subdivided its land holdings in exchange for the political support and tax payments of the nobility. The limitations on monarchical freedom to tax and otherwise abuse the nobility first occurred with King John’s (1199-1216) signing of the Magna Carta. It was then that the House of Commons, the archetype of all representative assemblies, held its first sittings.

By the 13th century, the basic features of the British system were in place: considerable freedom of property, freedom of contract, rule of law, parliamentary restrictions on arbitrary monarchical rule and enfranchisement of some of the propertied class. This is not to imply that the transformations of English society were smooth and graceful. There was considerable tugging back and forth between monarchical and parliamentary will. It was not until the Glorious Revolution of 1688, the dismantling of mercantilism in the 18th century and the expansion of suffrage through the series of Reform Acts beginning in 1832 that English society took on all of its 20th-century characteristics. The evolution of freedom in the United States followed a similar sequence.

The point is that private property and rule of law took hold long before political freedom. As noted above, in the 17th and 18th centuries, when a militarily superior England was exploring and colonizing a great deal of the world, it encountered cultures whose economic development was comparable to its own. The political freedom of representative government and universal suffrage that we know today is a 20th-century development. In 1870, only Switzerland had representative government based on universal male suffrage. Britain, the Netherlands and Belgium had parliamentary governments and competitive party systems, with suffrage based on property. Yet within 50 years universal suffrage was common not only in Western Europe but in the United States as well.

*“Part of the justification for free public schooling was the need to persuade immigrant children to accept American values and institutions.”*

**The U.S. Experience.** The first settlers in the United States were almost all expatriate Englishmen and thus adopted English institutions. Being labor-poor, we had a very liberal immigration policy. “Give me your tired, your poor” is the justifiably famous dictum on the Statue of Liberty. Yet immigration was a two-edged sword. We needed workers for our farms and factories, but we ran out of Anglo-Saxons. Irish, Germans, Scandinavians, Italians, Greeks and other Europeans came by the tens of thousands. Each had its own culture, some elements of which were thought to be inconsistent with American values. Part of the impetus for free public schooling in the United States, which began in the 1830s, was the desire to educate immigrants and their children in American values and institutions. We sought to homogenize immigrants — to make them speak English and disabuse them of radical political beliefs. In this regard, we were successful. But the desire to associate with one’s own kind dies hard. Many immigrants naturally segregated themselves (or were segregated) into areas with others of their own ethnic group. It is no accident that certain states have a predominant ethnic group or that large cities have ethnic neighborhoods.

In recent years it has become fashionable to cherish cultural differences, to teach the immigrants’ children in their native tongues and to withhold criticisms of different cultural values. Pluralism in today’s America assumes that all cultural values are equally valid. It should come as no surprise that America has become a Tower of Babel.

**The European Experience.** How have Europeans responded to the absorption of different cultures? Until the end of colonialism, there was no threat that immigration would undermine the dominant culture. A few immigrants, mainly educated ones, were granted residence in the colonizing country, where they were looked upon as curiosities. Since the end of colonialism, or for reasons of shortages of unskilled labor, significant numbers of foreigners have arrived in England, France, Germany and other European nations.

There are Indian, Pakistani and West Indian ghettos in London and other cities. But while most of the immigrants to Britain speak English and aspire to the English way of life, they are not well absorbed. Many feel they are victims of abuse and discrimination. The ethnic rioting in London, Liverpool and Manchester in 1981 was reminiscent of the urban riots in America in 1967. While the United States responded with the Civil Rights Act and group entitlements for minorities, the British responded by passing the Nationality Bill, which severely restricts further immigration from the former colonies, particularly India.

In France, there are now over three million Muslim Arabs. The French have vacillated between a policy of trying to make the Muslim Arabs French and leaving them alone. Where once Muslim girls wearing the traditional

black chadore were tolerated, now they are expelled from school. The French are so terrified of threats to their culture that they are even restricting American film imports.

For all its problems, the West has managed cultural conflict better than the rest of the world. The tension of absorbing different cultures through immigration has been partly diffused because of institutions that protect individual freedom and because attempts have been made to bring immigrants into the cultural mainstream. Nevertheless, many in Western Europe fear threats to the dominant culture from further immigration. Their reaction has been to curtail Third World immigration.

**The Experience Elsewhere.** In general, the institutions of the non-Western European world are less free. Part of the explanation may be cultural. Freedom as an idea never arose independently outside of the West. Nationalism has been used to defeat colonialism, socialism to transform the economies and religious fundamentalism to purge Western ideas in the Third World. But these forces have hardly contributed to free economic, civil and political institutions.

## Cultural Conflict

Cultural conflict has been described as “a struggle over values and claims to status, power and scarce resources, in which the aims of the conflicting parties are not only to gain the desired values but also to neutralize, injure or eliminate their rivals.”<sup>13</sup> Another scholar wrote, “In divided societies, ethnic affiliations are powerful, permeative, passionate and pervasive.”<sup>14</sup>

As many as half of all nations have experienced or are experiencing substantial cultural conflict in the second half of this century. Ethnic tensions (e.g., in the former socialist bloc nations, France), religious conflict (e.g., in Northern Ireland, India, Lebanon), racial friction (e.g., in the United States, South Africa, Malaysia) and linguistic differences (e.g., in tribes in Africa) have arisen.<sup>15</sup> They have made nation-building and intergroup cooperation quite difficult.

Colonialism and communism suppressed cultural conflict, forcing diverse populations into geopolitical units that free peoples might never have chosen. Now, many nation-states are disintegrating into smaller, more homogeneous political units. When the United Nations was founded, there were fewer than 50 nations. Now, there are more than 200. Cultural friction was an important force in the disintegration of the Soviet Union, Yugoslavia and Czechoslovakia. Separatist movements are widespread in Spain, Quebec, Sri Lanka, Indonesia, India, Pakistan, Turkey, Iraq, Sudan, Ethiopia, Ghana, Nigeria and Algeria. This fragmentation likely will continue.<sup>16</sup>

*“As many as half of all nations have experienced or are experiencing substantial cultural conflict.”*

*“Even if different groups live together peacefully, the lack of a common language and common norms reduces cooperation and increases the cost of transacting.”*

**The Role of Culture.** Culture includes learned patterns of behavior, socially acquired traditions, repetitive ways of thinking and acting, attitudes, values and morals. Cultural programming specifies rules for acquiring and transferring information. It standardizes perceptions. It also defines attitudes for intragroup relationships and for dealing with nonmembers. And it sets the institutional parameters that condition human behavior and stabilize social systems.

Culture standardizes relationships, so that people need not be constantly mindful of the implications of their behavior. They can make reasonably confident assumptions about the reactions of those with whom they interact. From the economist’s perspective, culture reduces transaction costs. The codes for interpreting external information, attaching values and priorities to that information, classifying forms of potential behavior as acceptable or not and perceiving social rank are all passed from one generation to the next through a system of reward and punishment. Successful cultural programming leads to ethnocentrism, a belief that one’s own culture is normal and, perhaps, superior. Frequently, other cultures are perceived as inferior.

**Culture and Conflict.** There are many dimensions of culture, but race, religion, ethnicity and language are the principal sources of diversity. When societies are multicultural, the ethnocentric differences of race, religion, ethnicity and language often lead to enmity. Enmity takes many forms:

- Violence (e.g., in Northern Ireland, Chad, Lebanon, India-Pakistan, Burundi, Indonesia)
- Separatism (e.g., Quebec, Swiss Jura, Belgian Flemings and Walloons, Berbers in Algeria)
- Terrorism (e.g., Sikhs, Basques, Corsicans, Palestinians)
- Expulsion (e.g., Chinese from Vietnam, Arakanese Muslims from Burma, Asians from Uganda, Beninese from Ivory Coast and Gabon)
- Ethnic rioting (e.g., in India, Sri Lanka, Malaysia, Zaire, Guyana)
- Ethnic control of the military (e.g., in Taiwan, Iraq, many countries in Africa)
- Political parties formed along ethnic lines (common in Asia, Africa and the Caribbean)
- Discrimination by the dominant group against others<sup>17</sup>

Even if different groups live together peacefully, the lack of a common language and common norms reduces cooperation and increases the cost of transacting.

As an economy grows, the distribution of resources is efficient but the resulting income distribution may be socially unacceptable. The government

redistributes income, sacrificing efficiency in the name of equity. Continuous income redistribution lowers economic growth through disincentives of various kinds, the withdrawal of productive resources into rent-seeking activities in the political market<sup>18</sup> and the lowering of capital formation.

**Homogeneous vs. Heterogeneous Societies.** In a culturally homogeneous society, redistribution of income by government is the main source of economic inefficiency and lowered economic growth. In culturally heterogeneous societies, intergroup conflict may result in additional economic inefficiency, lower the growth rate and even turn violent. Hostilities make property insecure, which slows the rate of capital accumulation. Eventually, in culturally diverse societies, one cultural group tends to dominate and to suppress violence and manage enmity. Domination may take the form of political authoritarianism, the suppression of civil rights and the control of economic resources. Manifestations of domination may include:

- Discriminatory restrictions on occupational choice (e.g., labor markets are ethnically segmented in parts of Asia, Africa and the Caribbean; trade unions often are ethnically exclusive; and civil service jobs, a large component of employment in the formal sector, often are the domain of an ethnic group)
- Denial of educational opportunities
- Licensing of trade
- Confiscation of land
- Nationalization of business
- Restrictions on property (e.g., Fiji Indians may not own land; it is difficult for Chinese to own land in Southeast Asia)
- Exchange and mobility restrictions

Where these cultural factors affect economic choice, technical, scale and allocative inefficiencies may follow.<sup>19</sup> In general, the restrictions imposed by the dominant cultural group on other groups denies them opportunities to compete for income streams. This denial leads to economic inefficiency.<sup>20</sup>

Anthropologists and social psychologists have found that group loyalty is widespread and leads to favoritism within the group and discrimination against those outside the group. In experimental games, members of a group tend to apportion more rewards to their fellows than to those not in the group. In games structured with three possible outcomes (i.e., maximize joint group reward, maximize ingroup reward and maximize the intergroup difference in reward), the most frequent outcome was to maximize the intergroup difference in reward.<sup>21</sup> This tendency for distinct groups to forgo intergroup cooperation and gains from exchange is harmful and economically inefficient.

*“Eventually, in culturally diverse societies, one cultural group tends to dominate.”*

## Cultural Diversity and Economic Growth

It is not my purpose here to argue that some cultures are better than others at producing a high standard of living for their citizens, although that may be so. My purpose is to show that cultural diversity within a nation may lead to a lack of personal freedom, which in itself contributes to a lack of economic growth. Much of the chaos in the Third World arises from the conflict between a dominant culture and minority cultures within the national borders. The dominant culture maintains power by controlling economic, civil and political institutions. Such control is associated with limitations on liberty.

*"Cultural diversity within a nation may lead to a lack of personal freedom, which in itself contributes to a lack of economic growth."*

Free markets, private property, rule of law and eventually representative democracy and universal suffrage arose in culturally homogeneous Western societies where *all* members of society had equal rights to compete in the marketplace. On the other hand, since control of economic resources is paramount to political control, dominant cultural groups structure economic institutions to serve their self-interest.<sup>22</sup> And when private property and economic rights are allocated along cultural lines, efficiency losses are inevitable.

There is empirical support for this view. I correlated the Freedom House measures of political and civil freedom (recall that they are ranked from 1 = most free to 7 = least free) with a cultural diversity index (measure from 0 = homogeneous to 100 = most heterogeneous) that is defined below. The correlation coefficients obtained with data on over 100 nations were .421 and .414, respectively. These correlations are statistically significant at the 99 percent level. It is fair to conclude that the more culturally heterogeneous the nation, the less is the people's level of civil and political freedom. The correlation with the economic liberty index (ranked from 0 = least free to 100 = most free) defined below is -.437. Thus the more culturally heterogeneous the nation, the lower the amount of personal economic freedom.

## Testing the Link Between Multiculturalism, Economic Freedom and Economic Growth

Using a model described in the appendix, we find that the effect of cultural diversity and of economic freedom on economic growth is substantial. The predicted growth rates for nations with various levels of economic freedom and cultural heterogeneity are presented in Table I.<sup>23</sup>

- The most economically free and most culturally homogeneous representative nation has a predicted growth rate of 3.07 percent per annum.
- The least economically free and most culturally heterogeneous representative nation has a predicted growth rate of .08 percent, a difference of nearly 3 percent per annum.

Another way of looking at these extremes in the growth experience of nations arrayed by the degree of economic freedom and cultural homogeneity is to calculate the number of years it would take to double the real standard of living.

- For the most free and culturally homogeneous nations, the standard of living would double about each generation.
- For the least free and heterogeneous nations, a doubling of the standard of living would take nearly a millennium. Various combinations of economic freedom and multiculturalism yield different predicted growth rates, as shown in the table and in Figure II.

## Conclusion

Cultural relativism has made the study of the role of culture in human progress controversial. But there is little disagreement that intergroup enmity is widespread in culturally heterogeneous societies. This paper shows that cultural diversity and a lack of economic freedom go hand in hand.

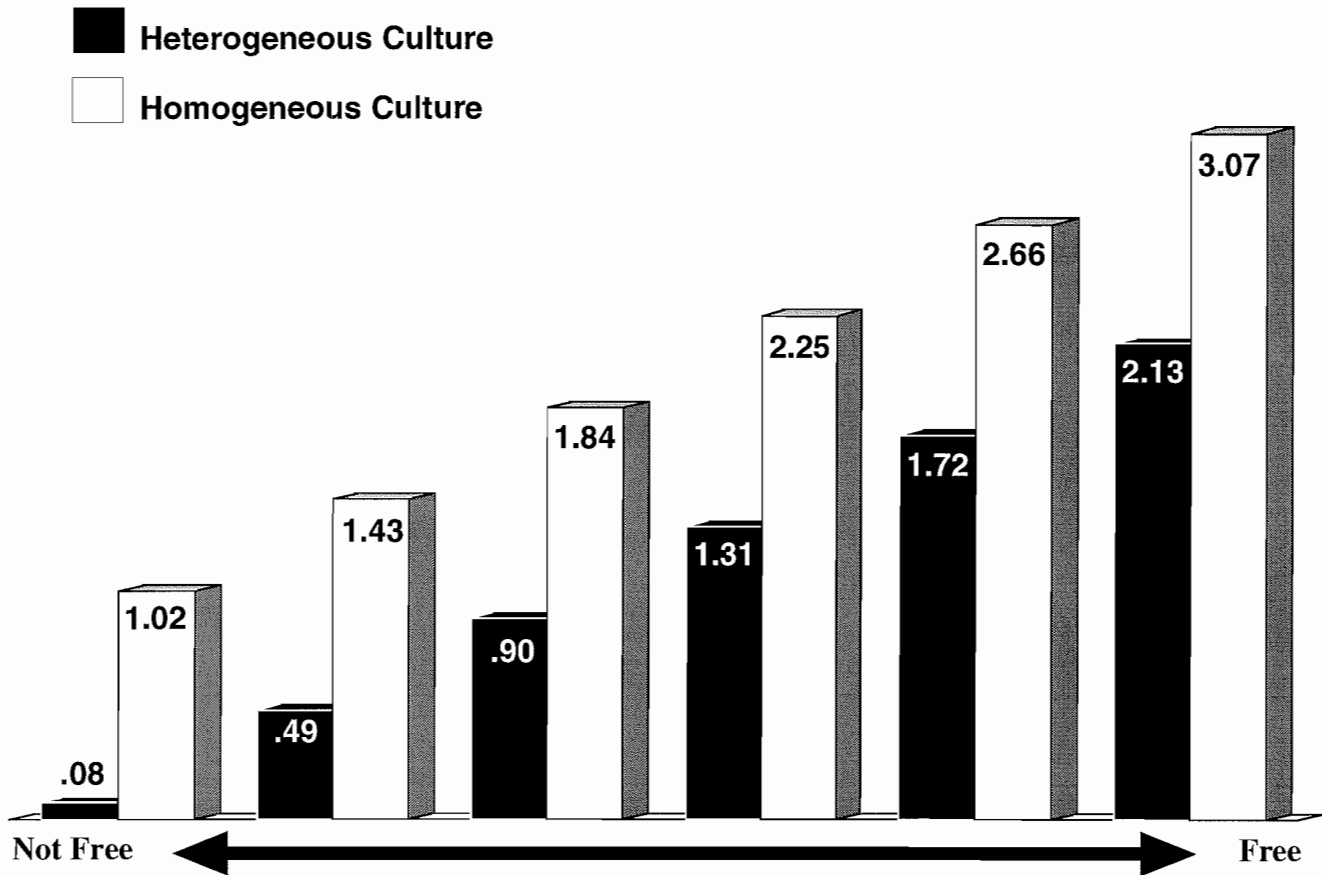
Because the West has free economic, civil and political institutions, multiculturalism has been managed better here than elsewhere in the world. Partly, the tension associated with the absorption of different cultures through immigration has been diffused because our institutions protect individual freedom. Partly, tension has been reduced through attempts to homogenize immigrants into the dominant culture.

**TABLE I**  
**Long-Term Economic Growth Rates**  
**Classified by Degree of Economic Freedom**  
**and Cultural Heterogeneity**

Culture	Economic Freedom					
	Free	80	60	40	20	Not Free
<b>Homogeneous</b>	<b>3.07</b>	<b>2.66</b>	<b>2.25</b>	<b>1.84</b>	<b>1.43</b>	<b>1.02</b>
20	2.88	2.47	2.06	1.65	1.24	.83
40	2.69	2.28	1.87	1.46	1.05	.64
60	2.51	2.10	1.69	1.28	.87	.46
80	2.35	1.91	1.50	1.09	.68	.27
<b>Heterogeneous</b>	<b>2.13</b>	<b>1.72</b>	<b>1.31</b>	<b>.90</b>	<b>.49</b>	<b>.08</b>

*"Cultural diversity and a lack of economic freedom go hand in hand."*

**FIGURE II**  
**Predicted Economic Growth Rates**



*"The standard of living rises far faster for more free and culturally homogeneous nations."*

Also, the scale of immigration is significant. Western Europe did very well with alien cultures when the number of immigrants was small. Since the 1960s, with decolonization, the number of immigrants has swelled. Immigrants are now as ghettoized in Europe as in America, and Europe is in a quandary about what to do if many immigrants from the former socialist bloc nations flee west.

There has been a sea change in the way the United States has dealt with the absorption of alien cultures. The intellectual roots of cultural relativism can be traced to what I call the "Four Men of the Apocalypse": Albert Einstein, Sigmund Freud, Margaret Mead and Dr. Benjamin Spock.

Einstein taught us that our fixity in time and space is an illusion. Matter, time and space are relative, not absolute, concepts. Freud taught us that our personalities are creatures of our desires and civilization's attempt to suppress them. Thus, there is no such thing as free will, individual responsibility or an absolute norm of desirable civility. Margaret Mead taught us that one culture is as good as another, and that we cannot assert the superiority of

Western culture to that of, say, African tribes that behead their enemies and mutilate their young women. Dr. Spock taught us that any infantile behavior in our children is acceptable. Thus, we as a society have lost confidence in asserting absolute standards of conduct.

Once we subscribed to the notion of the “melting pot.” A melting pot boils down disparate elements into a common substance — that is, it homogenizes. Now we have moved away from the notion of *individual* freedom to that of *group* rights. Perhaps the prototype of legislation specifically geared to groups is the Civil Rights Act of 1967. We recognized for a specific group (black Americans) a separate standing under the law. Women, homosexuals, the disabled, the vertically, calorically, folically challenged and so on have sought similar standing. Increasingly, ours is a country in which one’s standing before the law is a matter of group membership. Group membership gives specific rights and entitlements. But this is dangerous because emphasizing our cultural differences may exacerbate intergroup enmity and lead to social breakdown.

Outside of the West, cultural heterogeneity has caused social instability and retarded economic progress. A lack of personal freedom is correlated with the degree of cultural heterogeneity in many non-Western societies. More and more, scholars and Western politicians are recognizing that the key to economic transformation of the Third World is its movement to freer institutions. The cultural groups that dominate the economic, civil and political institutions of Third World nations fear the redistribution of wealth inherent in a shift to freer institutions.

Cultural heterogeneity is a major barrier to institutional reform and economic progress in the Third World.

*“The key to economic transformation of the Third World is freer economic, civil (legal) and political institutions.”*

NOTE: Nothing written here should be construed as necessarily reflecting the views of the National Center for Policy Analysis or as an attempt to aid or hinder the passage of any bill before Congress.

## Technical Appendix

In a 1988 paper, I analyzed the relationship between the rate of growth of real gross domestic product per capita over the period 1960-80, the rate of growth of the capital-labor ratio and various measures of the institutional framework (economic, civil and political liberty). In light of the above discussion, it is posited that economic growth is linked to capital accumulation, institutional choice and cultural and religious diversity. The growth equation to be estimated is of the form:

$$g_y = f(g_k, ECOFREE, DIVERSITY),$$

where

$g_y$  = the growth rate in real domestic product per capita over the period 1960-90;<sup>24</sup>

$g_k$  = the growth rate in real gross investment per capita over the 1960-90 period;<sup>25</sup>

ECOFREE = an index scaled from zero to 100 (most free) that measures the degree of economic liberty;<sup>26</sup>

CULTURE = an index scaled from zero (homogeneous) to 100 (most heterogeneous) that measures ethnic and linguistic diversity;<sup>27</sup> and

RELIGION = a binary variable equal to 1 if there is no dominant religion, and 0 if one religion overwhelmingly dominates.<sup>28</sup>

All of these variables are statistically significant (above the 99 percent level) covariants of economic growth. The simple correlations with the economic growth rate were: per capita gross investment growth rate (.691), ECOFREE (.614), CULTURE (-.427), and RELIGION (-.416).

In the previous paper, I treated the institutional framework as exogenous. Many researchers believe that institutional choice (e.g., free market vs. command allocation, representative democracy vs. authoritarianism) is endogenous. There is considerable debate about whether economic growth is determined by choosing institutions that protect individual freedom or whether the demand for freedom is a sort of luxury good that is aspired to after a certain standard of living has been achieved. We will treat the choice of the level of economic freedom as endogenous; that is, that such choices as free-market vs. command allocation originate internally. Thus the level of economic freedom is posited to be determined as follows:

$$ECOFREE = g(y_{60}, CULTURE, RELIGION, MUSLIM),$$

where

$y_{60}$  = real gross domestic product per capita in 1960;

MUSLIM = a dummy variable equal to 1 if it is the overwhelming majority religion and 0 otherwise; and the other variables are defined as above.

The simple correlations (all highly statistically significant) of these variables with ECOFREE are:  $y_{60}$  (.660), CULTURE (-.437), RELIGION (-.387) and MUSLIM (-.352).

The growth and the economic freedom equations are estimated jointly with three stage least squares. Two specifications are presented in the appendix table. In equation (1),  $g_k$  and CULTURE are exogenous variables and ECOFREE is endogenous; in equation (3), CULTURE and  $y_{60}$  are the exogenous variables. All of the coefficient estimates are of the correct sign and highly statistically significant. In equation (2), RELIGION is added as an exogenous variable. In equation (4), RELIGION and MUSLIM are added. It is known that countries with a Muslim majority are notoriously unfree.<sup>29</sup> About two-thirds of them are totalitarian, with little regard for rule of law.<sup>30</sup> The religious diversity and Muslim majority variables are highly statistically significant in the economic freedom equation, but their effect is to lower the statistical significance of the measure of cultural diversity. In the growth equation, the measure of cultural diversity remains statistically significant, but the religious diversity measure changes sign and is not statistically significant.

## APPENDIX TABLE

**Three Stage Least Squares Estimates (N = 110)**  
**(“t”-values in parenthesis)**

Variable	(1) $g_y$	(2) $g_y$	(3) ECOFREE	(4) ECOFREE
Constant	.533 (1.60)	.424 (1.26)	54.453 (11.29)	62.713 (13.14)
$g_k$	.283 (9.61)	.291 (9.48)		
CULTURE	-.895E-02 (2.51)	-.939E-02 (2.32)	-.229 (3.17)	-.118 (1.49)
ECOFREE	.193E-01 (5.19)	.25E-01 (5.47)		
RELIGION		.133 (0.50)		-16.854 (3.02)
$y_{60}$ 02			.723E-02 (7.75)	.555E- (5.98)
MUSLIM				-24.105 (4.39)
R <sup>2</sup> Adj.	.677	.677	.458	.538

## Notes

- <sup>1</sup> The standard explanation of the relative ease of European conquest and colonization is better armament. This also is a partial explanation for decolonization. Over time, arms became cheap and widespread, and the arms technology gap between Europe and the colonies shrank. Today, backward economies that devote a very large fraction of their gross national product to military purposes (e.g., India, Pakistan, North Korea, China) have developed atomic weapons and missiles.
- <sup>2</sup> Robert M. Solow, "A Contribution to the Theory of Economic Growth," *Quarterly Journal of Economics*, 70, 1956, pp. 65-94.
- <sup>3</sup> For a libertarian or Lockean, freedom of property and contract is absolute. During the 19th century, the United States, until about 1890, and England, until the passage of a series of Factory Acts, had near-absolute standards of freedom of property, freedom of contract and free market exchange.
- <sup>4</sup> Modern usage of civil rights includes an enumeration of human rights or entitlements that are to be given to those having the worthy characteristic at the expense of others in society. I do not include these redistributive rights (e.g., the right to a minimum standard of living, the right to a safe work environment) in my list of attributes of personal freedom.
- <sup>5</sup> Raymond D. Gastil, *Freedom in the World* (Westport, CT: Greenwood Press, various years). Early measurements of political and civil liberty suffered from limitations on source material, the comprehensiveness of the freedom measures and the attributes that made up the indexes of political freedom.
- <sup>6</sup> The most recent Freedom House survey has 38 percent of the nations of the world free, 33 percent partly free and 29 percent not free. Interestingly, Freedom House is beginning to acknowledge the role of multiethnicism and Islam on the lack of freedom. See Adrian Karatnycky, "In Global Vacuum, Tyranny Advances," *Wall Street Journal*, December 16, 1993, p. A18.
- <sup>7</sup> While there is a negative correlation between the degree of authoritarianism and civil (political) freedom, not all dictatorships are malevolent. For example, Singapore has a great deal of economic liberty and many civil liberties are protected. Yet political liberty is circumscribed.
- <sup>8</sup> Irma Adelman and Cynthia Taft Morris, *Society, Politics and Economic Development* (Baltimore: Johns Hopkins University Press, 1967).
- <sup>9</sup> Robert Summers and Alan Heston, "The Penn World Table (Mark 5): An Expanded Set of International Comparisons, 1950-1988," *Quarterly Journal of Economics*, May 1991, pp. 327-68.
- <sup>10</sup> Gerald W. Scully, "The Institutional Framework and Economic Development," *Journal of Political Economy*, 86, June 1988, pp. 652-62.
- <sup>11</sup> Recall that women did not get the vote until the 20th century. Also, in the 19th century, property qualifications were commonly a prerequisite to male suffrage.
- <sup>12</sup> Jeffrey A. Sluka, "The Anthropology of Conflict," in C. Nordstrom and J. Martin, eds., *The Paths to Domination, Resistance, and Terror* (Berkeley and Los Angeles: The University of California Press, 1992), p. 19.
- <sup>13</sup> Lewis Coser, "Conflict: Social Aspects," in D. Sills, ed., *Encyclopedia of the Social Sciences* (New York: Crowell, Collier and Macmillan, 1968), p. 232.
- <sup>14</sup> Donald L. Horowitz, *Ethnic Groups in Conflict* (Berkeley and Los Angeles: The University of California Press, 1985), p. 12.
- <sup>15</sup> Martin O. Heisler, "Ethnic Conflict in the World Today: An Introduction," in Heisler, special ed., *Ethnic Conflict in the World Today* (Philadelphia: American Academy of Political and Social Science, 1977), p. 1.
- <sup>16</sup> Economists have mixed notions of the relationship between size of nation and economic prosperity. One justification for size is based on economies of scale. That is, economies of scale depend on the size of the market. To the extent that cultural diversity creates economic inefficiency, there is a trade-off between size (economies of scale) and efficiency. Moreover, if free trade exists, domestic size of market becomes a less overriding consideration.
- <sup>17</sup> It is impossible to know what fraction of mankind has been affected by each of these forms of enmity. Mass murder and genocide are the most serious forms. By some estimates, from 170 to 360 million people have perished in this century from mass murder and genocide. In contrast, about 40 million died on the battlefield in this century's international and civil wars.

Not all mass murder is genocide. Communist China exterminated about 35 million of its citizens from 1949 to 1987, and

these were mass politico-economic murders. Perhaps 10 million of the 65 million state murders in the U.S.S.R. from 1917 to 1987 were genocide. On the other hand, almost all of the murders in Turkey (1.9 million, 1909-18), Poland (1.6 million, 1945-48) and Pakistan (1.5 million, 1958-87) were genocides. See R. J. Rummel, *Death by Government: Genocide and Mass Murder Since 1900* (New Brunswick, N.J.: Transaction Publishers, in press).

<sup>18</sup> Rent-seeking is trying to obtain through government action what one could not obtain for a good or service in the market-place.

<sup>19</sup> Technical, managerial or X-inefficiency is the failure to achieve maximum output for a given set of inputs (factor redundancy), holding allocative and scale efficiency constant. Scale inefficiency is the failure to produce an output at the cost-minimizing level, holding technical and allocative efficiency constant. Allocative inefficiency is the failure to choose the cost-minimizing input ratio, holding technical and scale efficiency constant. For definitions, see Philip K. Porter and Gerald W. Scully, "Economic Efficiency in Cooperatives," *Journal of Law and Economics*, Vol. 30, October 1987, pp. 489-512. See Scully, "The Institutional Framework and Economic Development," for the application of economic inefficiency at the macro level.

<sup>20</sup> Gerald W. Scully, "Rights, Equity, and Economic Efficiency," *Public Choice*, 68, 1991, pp. 195-215.

<sup>21</sup> For a summary, see Michael Billing, *Social Psychology and Intergroup Relations* (London: Academic Press, 1976), pp. 343-52.

<sup>22</sup> Marion J. Levy, *Modernization and the Structure of Societies: A Setting for International Affairs*, Vol. 1 (Princeton, NJ: Princeton University Press, 1966), pp. 68-70, 213.

<sup>23</sup> These were obtained by setting the investment and religion variables equal to their respective means.

<sup>24</sup> The description of the data is contained in Summers and Heston, "The Penn World Table." The data are available on diskette. Information was not always available for the 1990 observation. Of the 110 nations in the sample, the distribution of cases was: 1960-90 (84 cases), 1960-89 (19), 1960 to earlier than 1989 (6) and 1961-90 (1).

<sup>25</sup> Data on the gross investment share is contained in Summers and Heston. Investment shares were multiplied by real gross domestic product per capita to obtain real gross investment per capita. In Scully, "The Institutional Framework and Economic Development," the variable used is the growth rate in the capital-labor ratio. The correlation between the growth rate in the capital-labor ratio and the growth rate in real gross investment over the period 1960-80 for the 115 nations in the sample is .841. This is a sufficiently high correlation to justify the use of the growth rate of real gross investment per capita as a measure of capital accumulation.

<sup>26</sup> The economic liberty measure was constructed from various rankings of economic liberty obtained by principal components analysis or hedonic estimation of 15 attributes of economic freedom. See Gerald W. Scully, *Constitutional Environments and Economic Growth* (Princeton, NJ: Princeton University Press, 1992), pp. 106-47.

<sup>27</sup> The index is constructed from data in *Atlas narodov mira*, 1964.

<sup>28</sup> Data on the religious affiliation of the population is contained in *The World Factbook 1990*.

<sup>29</sup> See Scully, *Constitutional Environments and Economic Growth*, pp. 148-56.

<sup>30</sup> *Ibid.*, p. 162.

## About the Author

**Gerald W. Scully** is a Senior Fellow of the National Center for Policy Analysis and a professor of economics in the School of Management at the University of Texas at Dallas. His articles have appeared in the *American Economic Review*, the *Journal of Political Economy*, the *Journal of Law and Economics*, *Public Choice* and other scholarly journals. Dr. Scully is also an expert on the economics of sports. His most recent book is *The Market Structure of Sports*.

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