Social capital and prosperity

Searching for a missing link

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Recently, there has been growing interest in the link between social capital and economic performance. Social capital, it is claimed, is a complementary factor to other forms of capital and may help in raising levels of prosperity at the local and even national level.

The idea that social capital – understood as social networks, mutual trust and shared norms – is important for the working of the economy is certainly not new. It was the American political scientist Robert Putnam who made the concept known to a wide audience of commentators, scientists and policy makers. Many of them are eager to explore and promote social capital. The World Bank, for example, has set up a project on social capital hoping that it may stimulate civil society and economic growth in developing countries. European, national and local authorities often make use of the concept in regional development policy and urban planning. In economic and even management circles, debates on social capital have also become fashionable.

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Perhaps it has been the misty and nearly all-embracing definition of the concept itself that has contributed to its widespread popularity. No one seems to know exactly what social capital is, let alone how it works and how it may contribute, theoretically and empirically, to prosperity. By going back to the roots of the concept it might be possible to offer a new and meaningful perspective.

A chaotic concept

A shortcoming of popular concepts is that they are often ill-defined. As nearly everyone starts from a perspective grown out of their own definition and purposes, social capital has become an elastic and universal notion. Although he did not invent the concept, Robert Putnam popularised social capital in his influential work on regional development in Italy, *Making Democracy Work: Civic Traditions in Modern Italy* (1993). In this book he relates the differences between the rich north and the poor south to the degree of social capital. In this respect, Putnam defines social capital as 'features of social organization, such as trust, norms and networks that can improve

1070-3535/02/01052 + 04

the efficiency of society by facilitating coordinated action'.

In northern Italy there has been a tradition of voluntary co-operation and mutual trust that can be traced back to the Renaissance. The civic engagement and horizontal networks in this region, Putnam argued, have played a major role in overcoming collective action problems. Thus, social capital has improved efficiency and contributed to the region's successful economic development. Conversely, the lack of such a collective orientation in the southern part of Italy (the 'Mezzogiorno') should explain why this region is lagging behind. This line of argument brings Putnam to his statement that areas with a high level of social capital are conducive to economic growth.

Surprisingly, many economists saw the specific case of Italy as an expression of a general principle that social capital matters. In *The Economist*, Putnam's case study was even ranked as a 'great work of social science... alongside de Tocqueville, Pareto, and Weber'. Passionately, academics got busy exploring social capital and its effects at miscellaneous levels of scale. Immediately, however, they got stuck in problems concerning its definition and measurement. Putnam's original definition gave little hold as 'features of social organization, such as trust, norms and networks' leave much room for interpretation and discussion.

In an ultimate effort to clarify the concept, many researchers have resorted to statistics – including Putnam himself. In his latest book, Putnam (2000) floods his readers with all kinds of data to express his worries about declining civic and social activity in America. Likewise, his followers have reduced the rich and multidimensional notion of social capital to such limited indicators as political participation, membership of associations and the trust people claim to have in others.

For statistical analyses, researchers often rely on the World Value Studies, the Eurobarometer or other standard data sets that happen to be around. Data from these sources are usually connected to economic growth indicators such as the development of per capita income levels. At best, this statistical voodoo has resulted in inconclusive findings. For example, trust seems to matter in explaining economic differences between Nigeria and the Netherlands, whereas it loses significance when comparing western European countries or regions. But what strikes one the most in research on this issue, is that little attention is paid to the working of social capital in fostering economic development. What has a high membership of, say, the local soccer club or political party to do with economics?

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The standard approach

Usually, social capital is seen as an economic asset complementary to other production factors. The idea is that labour, physical capital and human capital do not suffice to explain economic growth. Social capital, it is claimed, is needed for the smooth operation of the economic process. It facilitates transactions and as such helps to optimise the use of other production factors. When people in a community trust each other, there is less need for legal rules and contractual safeguards. This, in turn, lowers transaction costs. In this way, social capital may save time and money. Moreover, participation of citizens in social networks stimulates collective awareness, which promotes information sharing and decreases the possibility of free riding.

There is much truth in this reasoning. In countries that have to cope with corruption and that lack a reliable legal system, doing business is no sinecure. Understandably, therefore, the World Bank has embraced the concept of social capital in the context of its development theory and policy. It is doubtful, however, if this argument makes sense in differentiating areas in the Western world in a meaningful way. As a matter of fact, social capital refers to rather fundamental characteristics of the economic process. One may expect that these basic conditions are met in industrial countries and regions – perhaps apart from extreme cases such as southern Italy. Here also, the question emerges as to whether social capital should be conceived as cause or effect. On the one hand it is conducive to economic development, but on the other, strong economic performance also proves the existence of social capital.

Even if we accept the standard line of reasoning, there are still many problems in making the alleged relationship between social capital and prosperity operational and measurable. As mentioned before, the variables and data sets that are used are highly limited and incomplete. Researchers often have to improvise in order to measure what they really want to know. Questions from questionnaires such as 'How much trust do you have in people from various countries?' certainly may give cause to socially desirable answers. Besides, what people say does not necessarily correspond to what they do. As a consequence, the conclusions from empirical research on social capital may be distorted significantly by the shortcomings in data gathering.

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Another problem is the choice of which scale level to study social capital on, in order to get relevant results. Basically, social capital refers to the 'property' of individuals to trust others and to co-operate with them. Is it possible just to stretch this concept from the individual to the aggregate level and re-label it to a feature of cities, regions and countries? Each scale level is made up of several groups that all have their own norms and networks. Within a region, for instance, there may be differences in social capital between inhabitants from cities and people from the countryside. It may not be so much social capital within a group that counts, but rather how different groups in a community get along. This observation puts social capital in a totally different perspective.

An alternative approach

Certainly, in contributions after *Making Democracy Work*, Putnam himself has recognised some limitations of his view on social capital. To overcome a few difficulties he has suggested a distinction between bonding and bridging social capital. The first concept refers to social capital within a certain group, while the latter concerns social networks between different groups.

By mentioning this incidentally Putnam nevertheless touches an important point. Interestingly, in a footnote in *Bowling Alone* (2000) he refers to Jane Jacobs as the scholar who introduced social capital as a notion. Paradoxically, it is her work that may help us in finding our way out from the current labyrinth surrounding social capital research. To Jacobs it is precisely the bridging elements of social capital that are crucial, as it is diversity that brings about vitality and prosperity. She argues (1961) that 'underlying any float of population must be a continuity of people who have forged neighborhood networks. These networks are a city's irreplaceable social capital'.

As this quote makes clear, Jacobs especially understands social capital as a feature

Two opposing views on social capital and prosperity

Social capital	*Robert Putnam*	*Jane Jacobs*
definition	features of social organisation such as trust, norms and networks	neighbourhood networks
character of relationships	emphasis on homogeneous elements	diversity and casual public contact
research method	mainly quantitative	qualitative
scale level	nations and regions	city districts
economic function	to lower transaction costs and facilitate co-ordination	to promote creativity, entrepreneurship and innovation
futuristic view	pessimistic	optimistic
policy implication	to bring about a Great Awakening	to contribute to diversity

of lively neighbourhoods within cities. Her ideas have influenced urban planners since the 1960s. At the age of 85 Jacobs still passionately advocates the importance of vibrant cities for economic life. Common sense, careful observation and personal experience are her guiding principles. Instead of juggling with models and statistics she prefers to go out herself and have a look in the streets of the city. Consequently, her work is not abstract, but rather deals with everyday life.

According to Jacobs, social capital emerges from and is maintained by diversity in various respects. Districts with all types of people in high densities (locals, immigrants, artists, business people), different functions (living, working and leisure) as well as a variety of buildings, ensure the presence of persons who go out at different times of the day for different goals. This diversity results in 'eyes on the street' which in turn creates safety, trust and a sense of civic responsibility. Moreover, the built environment can foster social capital by creating settings for casual public contact, such as public spaces, good sidewalks and neighbourhood stores. From a social point of view, Jacobs notes, it is not so much close contact within one particular group that is important, but rather sufficient public interaction on the street, near the bus stop or in the corner shop. All this turns a neighbourhood into a community and makes a city liveable.

Jacobs emphasises that diversity on the district level is also crucial for the flourishing of economic activity. Variety works like a magnet for entrepreneurs looking for opportunities and new combinations. In such an environment firms can meet suppliers and customers and they can draw knowledge and resources from each other. In this way, urbanisation economies that transform the district into a breeding place for creativity, entrepreneurship and innovation are generated. In interviews, Jacobs has referred to the social and economic vitality of Amsterdam as an example of a place in which she saw her ideas working in practice. To put it briefly, in Jacobs' view, social capital brings different people together in concentrations that are beneficial for the flourishing of a neighbourhood's community, commerce and culture.

What is to be done?

At present, social capital is widely seen as an important additional factor in explaining economic development. Unlike other forms of capital, social capital is an extremely ill-defined concept. In spite of – or perhaps thanks to – this ambiguity, many commentators, scientist and policy makers are exploring the link between social capital and prosperity. Most of them follow Putnam, an

American doomsayer who incites his countrymen to more civic and social activity or, as he puts it, a Great Awakening.

Putnam's findings and those of his followers are not only inconclusive, but also based on statistical juggling with inadequate indicators and incomplete data sets. These attempts to capture the concept of social capital and its economic effects can best be seen as walking down a dead-end road. Should we then forget about social capital? There is certainly no need for this, as long as one focuses on the right elements and scale of social capital.

It is Jane Jacobs, the founder of the concept, who shows us the way. In contrast to Putnam's approach, she champions social capital as the source of creativity, entrepreneurship and innovation in a city's districts. For Jacobs social capital does not imply homogeneity among members within a certain group. Instead, it depends on diversity in the neighbourhood and casual contact with other people. Unlike Putnam, Jacobs does not believe in apocalyptic scenarios forseeing the collapse of community. According to her it is natural for cities to have social capital and much can be done to keep or promote it.

Jacobs provides local governments with simple guidelines to stimulate diversity and socio-economic vitality. For example, they can create an environment in which city districts flourish by building adequate public spaces, mixing residential and working functions and mingling buildings that vary in age and condition. Therefore, really exploring social capital should start in your own street. So, do as Jacobs does: put on your tennis shoes, start walking and observe social capital as it is ●