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**Lecture 19: Culture and Overcoming the Dilemma**

1. What is culture?
   1. *Culture* is the norms or expected rules of behavior shared by a group of individuals.
   2. Culture can matter a great deal when doing business abroad (or even in different parts of the U.S.). Employees and business partners have certain expectations and if you ignore those expectations, you get a mismatch in action.
      1. For example, in many developing countries, something starting at 6pm in practice means people actually show up at 6:10, 6:30, or even 7pm. If you expect people to be exactly on time and they expect to show up ten minutes “late,” you’re going to have constant problems.
   3. It would be impossible to enumerate all the different ways culture can deviate from yours. My cousin-in-law, for example, teaches an entire class to Chinese professionals about Western etiquette.
   4. What we can do, however, is understand how to utilize cultural differences to your advantage.
2. The tragedy of the commons
   1. Recall from microeconomics that a commons resource (a resource everyone owns) tends to collapse as people over-use it.
   2. This is a prisoner’s dilemma game: each player can either harvest a little or harvest a lot. If they cooperate, the resource will be abundant. But each has an incentive to take more than what the resource can handle. By the dominant strategy, the resource is doomed.
3. Enter Elinor Ostrom
   1. Ostrom noted that many resources (river irrigation, pastoral lands, etc.) existed as a commons in many societies yet those resources survived. Those groups prospered.
   2. And it makes sense that the groups would be aware of the dilemma and try to overcome it. Some of these groups succeeded; that’s what Ostrom studied.
   3. Ostrom makes heavy use of *local knowledge*—knowledge of particular time and place—to explain the success of this institutions.
   4. She received the Nobel Prize in Economics in 2009 for her work in how institutions can successfully combat the tragedy of the commons. She passed away in June of 2012 of pancreatic cancer.
4. Culture in practice
   1. Ostrom’s work employs several case studies to demonstrate how resources can be managed successfully without regulation or privatization.
   2. She uses the term “common pool resources,” or CPR.
   3. In her landmark work*, Governing the Commons*, Ostrom outlines eight design principles for making sure a commons functions properly.
      1. *Clearly defined boundaries.* The CPR must have clear rules about who can use the resource. By closing it to “outsiders,” the gains from any investment are more certain and the potential for free riders is minimized. The game must repeat.
      2. *Congruence between rules and conditions*. How the CPR is allocated must fit with the local conditions. Irrigation systems that can store water via a dam, for example, allow for reliable information about how much water is available. Water use is thus auctioned off. Without storage, the water level is less certain and/or more scarce, the water is simply rationed. No single allocation rule is best everywhere.
      3. *Collective-choice arrangements*. Those who are affected by the rules are in a position to modify them. Conditions—population growth, weather patterns, increased or decreased erosion, etc—change so not only should the local populace be able to change the rules, these changes should be relatively easy to accomplish.
      4. *Monitoring*. Something we’ve discussed before: there must be some mechanism of detection when someone breaks the rules. Ideally, the rules should be structured so monitoring is cheap, thus we can ensure it’ll happen.
      5. *Graduated sanctions*. Some sort of punishment must follow the detection of non-cooperative behavior, with greater punishments for more serious violations.
      6. *Conflict resolution mechanism*. Even if you follow the letter of the rules, you might not follow the intent behind them. There must be a court-like system (even if it is manifested as social consensus and peer pressure) which corrects those who attempt to game the system or acknowledges a valid exception to the rules.
      7. *Independence from external authorities*. Governments and other authorities must recognize and allow these organizations to govern their CPR. Attempts to challenge these home-grown systems’ rule-making authority threatens the long-term survival of the CPR.
      8. *Nested enterprises*. If a community managing a CPR becomes too large to manage, it must allow subsets of the community to manage themselves (lest the community emulate a government). Much as politics is divided into the national, state, and local levels, this might require more than one level of nesting.
   4. Of all of these principles, numbers 3, 7, and 8 are perhaps most important to maintain since they are the ones that emphasize rule-making using local knowledge. All other components can come from those principles.
5. Implications
   1. Ostrom’s work not only highlights that the prisoner’s dilemma isn’t inevitable but how we in detail, we can avoid it. These ideas can then be applied elsewhere.
   2. Consider Wal-Mart
      1. Wal-Mart employees are empowered with the ability to order product. The company notes that the employees on the ground are in the best position to know what sells best for their store. Good relations between management and worker help ensure the worker will consider what’s good for the store.
      2. This is one reason why many retail outlets refer to entry associates as “team members.”
   3. Consider economic development
      1. Because these rules governing CPR’s are so important, they influence the culture and can replace “normal” approaches to property rights. This can be tricky when a non-local enters an emerging market thinking operations will be simple.
      2. Economists Hernando DeSoto was once wandering in the rice paddies of Indonesia. The only clue that he passed the boundary from one farm into another is that a different dog barked at him. They knew which assets their master controlled.
      3. Local ministers referred to these dogs as the “people’s law” and DeSoto suggested they use this local information to establish more formal property rights.