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Downsides of Social Capital

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COMMENTARY

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In their article, Levine et al. (1) test the hypothesis that ethnic homogeneity leads to greater errors in the pricing of stocks because of overreliance in the activities and decisions of coethnics. Excessive trust in others, created by ethnic homogeneity, can thus eventuate in price bubbles negatively affecting not only the traders, but the entire economy. The authors test this theory on the basis of two realistic, tightly controlled experiments comparing ethnically homogenous and heterogeneous trading networks. One experiment was conducted in North America, where the relevant ethnics groups were Whites, Latinos, and African Americans; the second was in Southeast Asia, with subjects of Chinese, Indian, and Malaysian origin. The distinctness of the ethnic groups compared in both settings adds to the generalizability of the findings.

The Communitarian Tradition

For a long time now, a tradition in the social science literature has deplored the loss of "community" and the advent of individualism, social atomization, and anomie. This literature features prominent titles, such as *The Lonely Crowd* (2), *Habits of the Heart* (3), and *Bowling Alone* (4). This tradition culminated in the celebration of "social capital"—defined as participation in associations and general trust in others—as an unqualified public good. Subsequently, Putnam (5) and his followers announced that ethnic diversity, brought about by heightened immigration, reduced social capital, hence negating the wide array of social benefits attributed to it.

This declaration received wide attention, scaring governments and members of the public alike. It resulted in a veritable mountain of research testing the relationship between immigration, ethnic diversity, and social capital. Almost entirely, this literature accepted the generalized positive effects of communitarianism and trust and focused on assessing the extent to which they were damaged by immigrant flows and diversity (6). Hence, the literature left the fundamental premises of the argument praising social solidarity and community bonds and disparaging individualism and impersonal rules intact.

There has also been, however, a less popular but equally important theoretical tradition that focuses precisely on the negative consequences of ethnic particularism and excessive reliance on community and trust. This tradition dates back at least to Max Weber (7), who made impersonality and universalistic rules in market transaction the key defining characteristics of modern rational capitalism, as opposed to earlier particularistic forms. The tradition also encompasses Durkheim's (8) distinction between mechanical solidarity, based on social homogeneity and tight personal bonds, and organic solidarity, based on role differentiation, impersonal norms, and an extensive division of labor.

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Negative Effects

More recently, other scholars in the same tradition have focused on the negative consequences of the much-celebrated social capital of which two deserve mention. First, as noted by Waldinger (9), the particularistic benefits accruing to some by virtue of membership in ethnic or religious communities is experienced by others as exclusion from the same social and economic benefits (10). Tight coethnic bonds allow the restriction of the best jobs to members of the in-group, thus requiring the intervention of impersonal public agencies to break up the holds of these bonds and open up opportunities for others.

A second negative effect of social capital consists of the excessive claims made on successful members of a particular community by others. As noted by Geertz (11) in his study of failed enterprise in Bali, the demands of kin and coethnics on successful business men can easily sink promising entrepreneurial ventures, preventing capital accumulation and turning firms into welfare hotels. Granovetter (12) identifies this problem as precisely the one that impersonal, universalistic markets were designed to resolve. The affinity of such markets to the Protestant Ethic was exactly the core of Weber's (7) analysis of the moral underpinnings of modern, rational capitalism. [A summary and systematization of the negative consequences of social capital are presented in Portes and Landolt (13).]

To these problems we can now add the one that Levine et al. (1) highlight. In this case, the negative consequences of social capital, in the form of excessive in-group trust, are felt not only by members of the group, but by the entire society in the form of market errors and bubbles, followed by stampedes (14). This result stems from the excessive confidence and comfort felt by market players in the presence of ethnically similar others and their consequent careless way of monitoring real market fluctuations.

These results have two other theoretical implications not discussed in Levine et al.'s (1) article. First, not only ethnicity but other bases of in-group solidarity and cohesion may produce exactly the same results. A common religious affiliation, common regional origin (i.e., "Southerner," "New Englander," and so forth), or even linguistic use and accent may lead to the same patterns of trust in others producing similar outcomes. Second, effects of excessive communitarianism may extend to areas other than the market. The political health of nations can be also affected. In this respect, it is worth recalling the warnings of Berman (15) following her analysis of the collapse of the Weimar Republic and the advent of the Nazi party to power in Germany. Berman (15) concludes her article, "Bowling with Hitler," on the following note:

> The German case reveals a distinct pattern of associationism that does not conform to the predictions of neo-Tocquevillian Theory. German civil society was rich and extensive—and this nation of joiners should accordingly have provided

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fertile soil for a successful democratic experiment. Instead, it succumbed to totalitarianism.

Undeniably, ethnic cohesion, solidarity, and trust have a number of benefits for communities and individuals. The economic success of certain immigrant groups, such as Russian Jews, Chinese, and Cubans could not be explained in the absence of such bonds (16, 17). Mutual trust among employers, labor unions, and the state has also played a well-documented role in economic "miracles" in Denmark, the Netherlands, and elsewhere in the recent past (18–20), but along with these and other benefits, social capital has severe downsides.

The unmitigated celebration of community, trust, and group cohesion in the social capital literature has cast aside impersonal regulatory institutions, universal norms, and self-reliance as key elements of markets and society. This result is regrettable because complex, modern economies can scarcely operate without such elements. As noted by Levine et al. (1), modern corporations do not run on social capital but on explicit rules and tight control of particularistic motives. Levine et al.'s article provides a valuable corrective to communitarian celebration; given the importance of its findings, they should be replicated with other groups and in other national contexts in the future.

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