

## THE AVAILABILITY OF SOCIAL CAPITAL IN TRANSFORMING ECONOMIES

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**Abstract.** *Today there is not a single country in the Balkans left that did not express the willingness to approach the western world, by accepting its economy, politics and society coordination principles. However, some of the transformation actors cannot claim any enviable success neither in economic performance nor visible progress in other areas of social life. Also, there is a fascinating variety in the accomplished transformation achievements, although the reformers have followed almost identical reform recommendations. This fact has lead to a thought that policy is not crucial for transformation success, but that social, political and cultural environment is equally important. Considering that the process of economic and political reforms is going on in a particular environment of specific societies, with their inherited habits, customs, traditions and systems of moral values, the final result is different in each particular country, according to its preconditions for a political-economic liberalization. These preconditions can be expressed in the form of social capital – a resource that encompasses society's norms of cooperation, reciprocity and trust, as well as social structures, like social networks, groups and associations which enable individuals to access social recourses. This paper deals with the problem of lacking social capital in transforming countries, and how it affects economic progress and the institutionalization of a new coordination system.*

**Key Words:** *Transformation, social capital, availability of social capital.*

The transformation of post-socialist economies has been going on for two decades and has shown fascinate variations in reform achievements in all fields – economic performance, political restructuring, social development. Since the reformers have been following very similar policy recommendations, such various reform results serve as a proof that policy measures are not more important than social, political and cultural environment in which the transformation is taking place. Each country has its own specific legacy of

moral values, social norms, habits and tradition, which pre-determine the course of political and economic liberalization. These cultural attributes of a society can be summed up under the concept of social capital, a synonym word for a social resource encompassing different features of social life – social ties, interactions, networks as well as norms and values embedded in these social structures.

The paper deals with the potential role that social capital can play in the course of political and economic transformation of post-socialist countries. Since there have been numerous attempts to resolve conceptual difficulties in understanding social capital, today there are many different, even contradictory explanations of this phenomenon. Therefore, the first chapter deals with conceptualization issues, in order to make distinction between dimensions, sources and effects of social capital. The next chapter investigates under which conditions social capital can produce beneficial outcomes in the society, pointing out to several areas in which social capital can be an important determinant – social exchange, public goods provision and economic performance. Finally, the last chapter addresses the problem of social capital availability in transforming countries, trying to find out the reasons for its absence and ways to facilitate its accumulation.

#### SOCIAL CAPITAL – DEFINING EFFORTS

In order to understand the ways social capital determines social outcomes, especially economic activities and performances, it is necessary at least to try to resolve conceptual difficulties associated with social capital ever since it was introduced into social science [see more in Golubović, 2007: 30]. Once the essence of the concept is understood and its key elements identified, attention can be focused on unfolding the very effects this social resource produces in economy or society at large.

Social capital has turned out to be one powerful and popular metaphor in social science researches. Mostly addressed as a system of community ties that define personal interactions, this concept is used for explaining a very wide range of different phenomena – from voter behavior patterns to country's economic performance. The importance of social capital is being confirmed by a vast amount of literature that indicates its role in explaining different levels of social efficiency [Durlauf and Fafchamps, 2004: 9]. Officially, the concept of social capital has first been brought to light in sociology, but it soon spread throughout the social sciences. In spite of an immense amount of research, the definition of social capital has remained incomplete. It can even be admitted that social capital is more of a federating concept that captures different ideas and phenomena inside it. Such conceptual vagueness is an initial obstacle on the road of explaining its effects on various social outcomes. This is why, depending on the discipline or the author, the term social capital serves as a code word for: social networks, structures or groups, community ties and interactions, social norms, trust, cooperative behavior and informal institutions. It is interesting that economic science does not own the exclusive right of studying this phenomenon, but the problems of its conceptualization have for a long time existed in sociology as well as in the political science. Its interdisciplinary character is confirmed through the forms of its appearance, as well as the effects it exerts in different spheres of social life.

One of the first accepted conceptualizations of social capital originates from the sociological science, as Coleman in one of his pioneer works on the subject defines it as a component of human capital that allows members of given society to trust one another and cooperate in the formation of new groups and associations [Coleman, 1988: 98]. A few years later, Putnam in his revealing work that has aroused much publicity among scholars, defines social capital as encompassing features of social life – networks, norms and trust that enable participants to act together more effectively to pursue shared interests [Putnam, 1993: 167]. Economists see social capital as knowledge, networks and reputation as social means to handle issues of individual incentives and motivation [Stiglitz, 2000: 59]. Generally speaking, all these definitions refer to trust, cooperative behavior and networks between groups, as elementary components of social capital. It is not yet resolved whether trust is a component, source or a consequence of social capital, but it appears in different forms: as interpersonal – trust acquired through repeated interactions between familiar subjects: generalized – trust in unfamiliar people, other than close friends and family members; and trust in public institutions. The last two forms of trust are considered crucial in strengthening and intensifying social ties.

Broadly speaking, social capital can be understood as a network of different social relations based on various forms of trust and reciprocity that can lead to a wide range of public and private outcomes. However, especially important for studying the specifics of transforming societies is the distinction between two significantly different conceptual and methodological approaches [Mateju, Vitaskova, 2005: 2]. The first one defines social capital primarily as an attribute of an individual, referring to a person's potential to activate and effectively mobilize a network of social connections based on mutual recognition of shared interests. In this context, social capital has the properties of a private good, accumulated by individuals, that they use to achieve their own goals and personal advancements. The second approach considers social capital mostly as an attribute of a society, as a quality of networks and relationships enabling individuals to cooperate and act collectively. Within this framework, social capital is based on a high degree of interpersonal trust, as well as on the trustworthiness of public institutions that establish and uphold the rule of law, making all kinds of transactions transparent and safe. According to this approach, social capital is a synonym for the level of civil consciousness in society, presence of social norms that enhance collective action and trust in public institutions. For these reasons, social capital has all the properties of a public good, facilitating achievement of higher levels of efficiency and productivity; hence this form of social capital is often associated with economic growth. That is why economists, who are searching primarily for the factors accounting for differences in economic growth and economic well-being of nations, often tend to prefer interpretation of social capital as a public good, while sociologists, who are striving for an explanation of reproduction of inequality, incline to conceptualization of social capital as a private good. From these definitions, we can distinguish the following main underlying ideas: social capital generates positive externalities for members of a group; these externalities are achieved through shared trust, norms, and values and their consequent effects on expectations and behavior; shared trust, norms, and values arise from informal forms of organizations based on social networks and associations.

## ECONOMIC EFFECTS OF SOCIAL CAPITAL

Speaking about potential influences social capital may have on socio-economic outcomes, it is necessary to point out that these influences need not be purely positive, since strong social connections can lead to immoral or unproductive behavior. Likewise, the benefits social capital can bring to some individuals inside a certain group may turn out to be costs imposed to the non-members, so the overall effect on social efficiency need not be positive. Therefore, it is of huge importance to determine under what conditions social structures generate beneficial outcomes.

Recent scholar researches on social capital agree on the fact that social capital's most important role is to be the factor that ameliorates potential inefficiencies caused by information asymmetry, as an inevitable attribute of human society. Information asymmetry limits social exchange in the way that potential exchange actors cannot find each other or do not trust each other enough to make the exchange. Therefore, the efficiency of social exchange is mostly determined by the mechanisms of information sharing and the degree of generalized trust in the society. The role of social capital in raising social exchange efficiency is in improving interpersonal connections in order to raise the level of trust and reinforce the ties within social networks. The illustrative example of social capital achieving this goal is channeling information about jobs and workers in the labor markets. Unlike stock markets, where potential buyers and sellers can easily find information about the object of exchange, labor market does not have an equivalent institution which circulates accurate and up-to-date information about available jobs or potential employees. The main role here is played by interpersonal relationships in channeling important information, so a large proportion of jobs are allocated on the basis of personal recommendation and word-of-mouth. This can be understood as an endogenous, spontaneous adaptation to the absence of a formal clearing house equivalent to the stock market. This comparison does not constitute evidence that social capital is necessary and should be nurtured. Depending on the circumstances, the development of formal institutions may be a superior alternative [Granovetter, 1995: 128].

Analyzing other areas of social exchange where social capital can make desirable effects, we come to the fact that trust is an essential ingredient in the delivery of public goods. Whenever it is not possible to organize such activities through taxing individuals and state intervention, trust becomes essential. In poorer countries where state's tax base and capacity are limited, collective action can serve as a substitute for state intervention. However, the absence of the state's coercive power makes collective action much harder to organize, so two more essential ingredients are required: leadership and trust. A leader is required who is capable of convincing community members that they should voluntarily contribute to the public good, while trust is necessary to resolve conflicts among competing interests and to reduce fears of free-riding.

Apart from the effects on the exchange efficiency and public goods provision, social capital is able to produce certain distributive effects and that way affect the level of social (in)equality. If the benefits of social capital principally accrue to network members, those who happen to be included benefit from increased efficiency but those that are excluded are penalized. This case appears whenever the members of a network or a group stop contacting non-members due to easier inter-network communication. Negative effects on equity appear mostly when membership is restricted or new members are not accepted.

Even when new members are accepted without restriction, equal opportunity need not be realized because old members have enjoyed the benefits of membership for much longer. Investing in social capital by promoting such closed networks can thus have serious equity repercussions, generating social polarization and political tensions. Also, it cannot be ignored that some groups are in the first place created in order to dominate or exclude others. Therefore, depending on the incentives that govern network activities, social capital accumulation can have various effects.

Both approaches, that define social capital as public and as private good, claim that social capital facilitates economic exchange. The mechanisms through which this is achieved are, however, significantly different. Social capital as private good can facilitate economic transactions between individuals, even though it can sometimes impose costs to other agents. Its effect on the overall economic results of a society is therefore uncertain and potentially negative. On the other hand, the public good concept of social capital points out a positive impact of individuals' involvement in social life, their feeling of civil duties, and efficiency of existing institutional arrangements on the efficiency of economic transacting. Moral obligations are infiltrated into social connections system and civil participation facilitates formal rule enforcement and stronger state responsibility. In that sense, social capital is complementary to formal institutions that regulate society's labor division. Its effect on the economic performance should inevitably be positive.

The economic payoff of social capital is most clearly summarized in Knack and Keefer [Knack, Keefer, 1997: 1252], who begin their analysis with the famous conclusion of Kenneth Arrow: "Virtually every commercial transaction has within itself an element of trust, certainly any transaction conducted over a period of time. It can be plausibly argued that much of the economic backwardness in the world can be explained by the lack of mutual confidence". That is why economic activities that require agents to rely on the future actions of others (future payments, accomplishing tasks difficult to monitor or assurances by governments that they will not expropriate savings or investments) are accomplished at lower cost in high-trust societies. A high level of trust reduces the costs of protecting individuals from opportunistic behavior of other agents, or protecting investors from possible malfeasance, so that they can spend more resources on their innovations. In the societies with higher trust level, enforcement of agreements and protection of property rights is less dependent on formal institutions. Higher investment and other economic activity is also triggered by greater trustworthiness of government officials and credibility of their policies. In such societies, economic agents are able to make decisions that are optimal in the long, rather than short run. Apart from stronger incentives to innovate and accumulate physical capital, high trust societies tend to invest more in human capital. High trust improves credit access to the poor; enrollment in higher education is increased and hiring decisions become more influenced by personal attributes of applicants, rather than personal ties and friendships.

#### THE SPECIFIC NATURE OF SOCIAL CAPITAL IN POST SOCIALIST ECONOMIES

There are significant differences between both the level of social capital in advanced economies and its impact on economic activity, compared to post-socialist countries that are burdened with their legacy from the previous regimes and their day-to-day struggles

with the problems of reform implementation. The studies of possible dictator regime consequences on social capital in the course of transformation as well as considerable presence of informal networks and institutions in transition countries call for acknowledging specific conditions of social capital existence and economic effects. As post-socialist societies have been facing accelerated institutional changes in order to adapt to market and democracy requirements, adjusting formal and informal institutions has caused enormous uncertainty, instability of agents' expectations and unpredictability of their behavior. Due to specific historical and social conditions, the understanding of social capital as a social environment based on interpersonal trust and cooperative behavior directed to common goal achievement is no longer sustainable and cannot contribute to the explanation of economic performance, as it is the case in relatively stable societies with developed institutional and political infrastructure [Mateju, Vitaskova, 2005]. In transforming societies, whose essential infrastructure, owing to recent changes in political systems, is underdeveloped and trust in the state is low, social capital can best be described as a system of mutually beneficial exchanges based on social ties and informal networks that enable individuals to accomplish their goals. In that sense, the specificity of social capital in transforming countries, comparing to advanced market economies, displays mostly as it is perceived as individual capacity for participating in informal networks based on mutually beneficial exchanges, and not as the feature of social environment that enhances cooperative behavior.

Several factors have caused the appearance of such specific character of social capital in analyzed countries. First of all, most of these states can be identified as *weak*, in terms of decreased legitimacy, which appears as a consequence of various functional problems – the state is not able to provide basic services to the citizens (the rule of law, contract enforcement, and public health and education services). Such low level of government functionality is supplemented by certain government failures that depict the state as the source of different problems: corruption, arbitrary law enforcement, even the involvement of state apparatus in criminal structures [Fritz, 2004]. The prevalent opinion is that the weak state is inherited from the socialist period, considering that the initial power of communism has faded in time, so in the last couple of years the communist state has already largely been permeated by black-market trading, meaning that even before its dissolution it has lost a significant degree of control over the final allocation of resources and was concerned more with the allocation of rents among public servants [Olson, 1993]. The legacy of a weak state and the use of public office for personal gains continue to retain a strong impact on institutional performance in many of the post-socialist countries. This impact exerts in two different ways: on one hand, there is continuing discrimination against private businesses through remaining bureaucratic distortions; on the other, there is the transformation of former black-marketers into legal businessmen acquiring substantial domestic resources [Reiser, 2007]. However, what undermines state legitimacy most is the reform outcome, more precisely the gap between reform goals and achieved results [Joksimovic, 2007]. Diminished state credibility has caused informal norms to become increasingly important as a coping mechanism in times of uncertainty, which contributed to the deepening of inherited distrust in the state and formal institutions from the socialist period.

Described events also had certain implications for the various forms of social capital. Social (political) trust that relates to trust in institutions was the one form that suffered the

most. The studies that explore the levels of corruption and rule of law in different countries throughout the world indicate that transition countries face the most intensive problems of this kind. In other words, communism seems to have left as legacy the perception that while each individual might profit from informal social capital, private returns to civic participation and other forms of formal social capital would be low [Reiser et al., 2007]. Facing numerous injustices, irregularities and abuses during the process of political and economic reforming, the citizens ceased to believe that government structures act in public interest. Surveys indicate that the last atoms of citizens' trust are absorbed by repressive institutions – the ones that provide law and order, as well as traditional institutions, like church, while the structures that are most in need of legitimacy, being the bearers of the reform process (politicians, parliament, government) are not trusted at all [Joksimovic, 2007].

The situation with generalized trust, as trust in anonymous individuals based on limited information about their attributes, is not much better, considering that distrust in the state and law reflects on the individual perceptions about trusting strangers. The World Values Survey data indicates that in the last couple of decades the level of generalized trust noticeably decreases in the countries that follow the East-European development patterns, unlike post-socialist countries that are turned towards the West. This can be related to deep changes in social structure of transforming countries, followed by increasing social and economic inequalities and changes in the processes of social stratification. Additional contribution to undermining of generalized and political trust was the general perception that individuals belonging to elite social groups, which have widespread political and social connections, are above the law and that the law acts purely in the interest of these status groups. Such groups have privileged access to markets, are experienced in conducting informal procedures and are capable of bypassing formal rules and procedures. Special treatment of certain groups before the law subverts social solidarity encapsulated in generalized trust and could lead to loss of safety and trust in neutrality of state institutions [Joksimović, 2007]. These are obvious reasons for strengthening informal, particularistic networks as rational compensation for inefficient formal institutions. In times of social changes, individuals who understand that their potentials depend on their position in society, rationally tend to become a part of a status group, rather than act to change the rules. An interesting metaphor for such image of a transforming society is an "hour-glass society" [Rose, 1995]. In the communist regime, the individuals have created network of close mutual relations within close friends and family, rarely going out of this well-defined circle. This part of the population has formed the bottom of the hourglass, while at its top were the similarly closed circles composed of the privileged, powerful and few members of the "nomenclatura", with very little interaction between these two levels. Social circles in transforming societies are therefore much firmer and closed-up compared to advanced economies, while the relation between informal social capital (relations between friends, for example) and general moral attitudes is not clearly defined.

#### CONCLUDING REMARKS

It is a familiar fact that informal norms have a more significant role during society's transformation, since they have been continuously repressed in the previous regime. The

inherited system of informal values and norms in combination with the direction of institutional change has a large effect on the course of reform outcomes. The role of social capital in transformation can be interpreted mostly as determining the way citizens accept new modes of economic transacting, as well as intensifying their active participation in social life. Therefore, social capital is recognized as a determinant of economic progress as well as democratic consolidation in transforming countries. The ways individuals connect in order to pursue both individual and communal interests, can to a great extent determine the outcomes of social activities. Since transforming countries choose liberal democracy as an environment for resolving economic issues, the level of social capital might be one of the most significant factors of establishing a healthy and stable political framework for governing the society.

The main problem about social capital in transition countries is how to determine its availability, which is supposed to be insufficient, and more importantly – to find the causes of such insufficiency. A large amount of guilt is intuitively ascribed to fallen communist regimes, so there are a growing number of accusations that authoritarian regime or, more precisely, dictatorship destroyed social capital, by diminishing interpersonal trust and trust in state institutions, while discouraging any form of citizen political and social participation. Besides, the previous regime is assigned the responsibility for the occurrence of semi-legal social networks, which turned out to be the only surviving social mechanism in repressive conditions. These informal networks have taken over the coordination of economic exchange, resolving it through barter arrangements, enterprise networks, transactions in grey and black economy. It is supposed that the abolition of communist dictatorships has not been followed by destruction of such informal networks, but on the contrary, they have continued their function after the regime shift, contributing the spread of corruption and other illegal activities of economic and political subjects. On the other hand, there is a reasonable possibility that the lack of social capital is a result of a slow economic development and weak institutional infrastructure in the transforming period. No matter what the cause is, missing social capital could be at least partly responsible for slowing down the reform and a lapse in its full implementation.

The observed lack of social capital is mostly referred to the reduced level of trust. When a state is transforming from dictatorship to democracy, the process of building trust between citizens and the state is running quite slowly – citizens do not trust the state and government officials do not confide in the citizens and their ability to participate rationally in the political life. Spreading grey economy, corruption and dishonest behavior can probably be considered a consequence of distrust. In that sense, raising the level of trust between the citizens and the state is one of more important policy issues, so the main question is how to achieve it. Some of the suggestions for restoring trust in government institutions are to enhance citizen participation in the political decision-making process. It is yet unknown whether the voters in recently established democracies are capable and eager for such activities.

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## RASPOLOŽIVOST SOCIJALNOG KAPITALA U PRIVREDAMA KOJE SE TRANSFORMIŠU

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*Danas ne postoji nijedna zemlja na Balkanu koja nije izrazila spremnost da se približi zapadnom svetu, kroz prihvatanje principa koordinacije ekonomskog, političkog i društvenog sistema. Međutim, neki od aktera transformacije ne mogu se pohvaliti zavidnim uspehom ni po pitanju ekonomskih performansi ni po uočljivom progresu u ostalim oblastima društvenog života. Takođe, iznenađujuća je raznolikost ostvarenih rezultata transformacije, iako su reformske politike različitih zemalja zasnovane na skoro identičnim preporukama. Ove činjenice ukazuju da mere ekonomske politike nisu presudne za uspeh transformacije, već da pažnju treba posvetiti i društvenom, političkom i kulturnom okruženju u kojima se one sprovode. Imajući u vidu da se proces ekonomsko-političkih reformi odvija u specifičnom okruženju društava sa nasleđenim navikama, običajima, tradicijama i vrednosnim sistemima, konačni ishodi razlikuju se od zemlje do zemlje, u skladu sa njihovim preduslovima za sprovođenje političke i ekonomske liberalizacije. Jedna od formi u kojoj mogu biti iskazani pomenuti preduslovi jeste raspoloživost socijalnog kapitala – resursa koji objedinjuje društvene norme kooperacije, reciprociteta i poverenja, kao i društvene strukture, poput društvenih mreža, grupa i asocijacija koje pojedincima omogućavaju pristup društvenim resursima. Ovaj rad se bavi problemom nedostajućeg socijalnog kapitala u zemljama koje prolaze kroz transformaciju i načinom na koji ovaj problem utiče ekonomsko napredovanje i institucionalizaciju novog sistema koordinacije.*

**Ključne reči:** transformacija, socijalni kapital, raspoloživost socijalnog kapitala