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UNDERSTANDING SOCIAL INCLUSION, SOCIAL COHESION AND SOCIAL CAPITAL

ROB OXOBY*

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* Department of Economics, University of Calgary.
Contact: oxoby@ucalgary.ca

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Robert J. Oxoby[†]

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Abstract

The topics of social capital, social cohesion, and social inclusion are increasingly gaining interest in economics, sociology, and politics, particularly in regards to addressing poverty and designing related policies. Here, we seek to develop the connections and interdependencies between these related concepts. We offer a framework for understanding the differences between these concepts and how they fit together in individual decision making.

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[†]Department of Economics, University of Calgary, 2500 University, Drive NW, Calgary, AB Canada T2N1N4, tel: 403.220.2586, fax: 403.282.5262; email: oxoby@ucalgary.ca.

> I am an invisible man. No, I am not a spook like those who haunted Edgar Allan Poe; nor am I of your Hollywood–movie ectoplasms. I am a man of substance, of flesh and bone, fiber and liquids — and I might even be said to possess a mind. I am invisible, understand, simply because people refuse to see me. Like the bodiless heads you see in circus sideshows, it is as though I have been surrounded by mirrors of hard, distorting glass. When they approach me they see only my surroundings, themselves, or figments of their imagination — indeed, everything and anything except me. (Ellison, 1952)

1 Introduction

The main character in Ellison's classic novel is the epitome of the excluded individual. Gifted and talented, he finds the doors to society's institutions closed to him (or, more accurately, slammed). As a result, he opts to lead a life in which he is invisible, unnoticed by those around him and forgotten by those who knew him. In modern society, he may represent the poor, the disenfranchised, or those individuals whose decisions and skills have been marginalized.

While traditional economics research has focused on productivity and factor endowments in determining growth and development, there is increasing recognition that the ingredients for a proper functioning economy (i.e., one experiencing higher levels of growth and individual well-being) are perhaps more subtle. Thus, researchers have turned their eyes towards the issues of social capital and social cohesion, trust and trustworthiness, and reciprocal altruism in understanding economic performance.

Ellison's invisible man highlights another important ingredient in a successful economy: Ellison's character considers himself excluded from social and economic opportunities, and therefore vanishes from the typical realms of economic behavior. That is, he experiences economic exclusion, perceiving the world as discriminatory and denying him his full potential. This interpretation suggest that successful economic policy minimizes the extent to which individuals perceive themselves as excluded. While not necessarily the opposite of exclusion, economic and social inclusion (generally characterized as a situation in which individuals are integrated into the economic, social, and political framework of society) are increasingly viewed as essential in developing successful growth strategies, fighting poverty, and increasing well-being in an economy. While most discussions of inclusion and exclusion focus on those individuals living in poverty, these issues go beyond economic means, affecting all citizens and the efficacy of economic and political policy.

In this paper, we present several definitions of social capital, cohesion, and inclusion which are quite different from those used in the existing literature. Our goal is to develop a taxonomy of these concepts that allows us to disentangle their effects in economic and social realms. After defining these concepts, using the work of Amartya Sen and others as a foundation, we discuss the theoretical and empirical research in this area.

2 Defining Inclusion, Cohesion and Capital

Before we begin considering the roles and effects of economic and social inclusion, it is useful to consider the definitions of inclusion and its related concepts (social capital and social cohesion). While the concept of inclusion has been used as a user-friendly term addressing the manner in which individuals can access resources and institutions to their benefit, the absence of a formal definition poses significant problems to research in this area. Moreover, the lack of a formal definition for inclusion (and its related concepts) poses significant problems in trying to move research findings into policymaking. This has led some, notably Arrow (2000), to suggest these terms be abandoned and that research focus be shifted to studying specific social interactions.[1]

In terms of economics research, while the literature has explored issues of social capital (e.g. Glaeser et al., 2000, 2002) and social cohesion (e.g. Gradstein and Justman, 2002), there is far less economic research on the issues of inclusion and exclusion.[2] Indeed, this relative paucity of research on inclusion and exclusion is largely due to the lack of clear definitions for the relevant concepts. As discussed by Atkinson (1998), the term social exclusion "seems to have gained currency in part because it has no precise definition and means all things to all

[1] Others (e.g Brady, 2003) have suggested more strict definitions of exclusion and inclusion, seeking to develop a more meaningful understanding of poverty and related problems.

[2] Notable exceptions include Atkinson (1998) and Phelps (2000).

people."

That said, there does exist (broadly speaking) a general consensus on the meaning of social and economic inclusion/exclusion. For example, discussions of exclusion tend to focus on the phenomena of poverty, unemployment, low educational attainment, and barriers to social and political institutions. Under the rubric of inclusion, discussions focus on access to (and relative success with) economic, social, and political institutions. Moreover, individuals speak of policies which emphasize inclusion by opening institutional doors and allowing all individuals the opportunity for freedom of expression and decision-making.

Using the ideas of Sen (1985, discussed in section 2.2), inclusion and exclusion deal with the success or failure of attaining proper functioning and developing capabilities that are deemed valuable in an economy. Thus, the concepts of inclusion and exclusion are multidimensional, involving more than the concepts of poverty and inequality. However, the absence of clear definitions has resulted in research focusing on the polar concepts of inclusion versus exclusion and on extreme cases of economic exclusion (namely extreme poverty; see Avramov, 2002; O'Flaherty, 1995, 1996). While poverty may be a result of exclusion, exclusion is not simply poverty. For example, exclusion can lead to the abandonment of mainstream norms (Lafree, 1998; Liebow, 1967) and the development of separate subcultures (Hagan and McCarthy, 1998; Oxoby, 2004). Similarly, exclusion (while potentially leading to non-participation in the labor market; Atkinson, 1998) may also manifest itself in withdrawal from social and political life (Putnam, 2000). Thus, the effects and manifestation of exclusion may be highly nuanced.

Here we attempt to present definitions related to inclusion and its related concepts. Our goal here is to present definitions that will focus and target theoretical developments and the types of empirical data necessary to further our understanding.[3]

[3] This approach is different than the axiomatic approaches to characterizing measures of inclusion and exclusion found in the work of Bossert et al. (2004), Bourguignon and Chakravarty (2003), Chakaravarty and D'Ambrosio (2003), and Estaban and Ray (1994, 1999) where the emphasis is on devising indices for the measurement of inclusion and exclusion.

2.1 Defining Social and Economic Inclusion

It is perhaps because of the complexities in economic and social exclusion that no precise definition exists. Indeed, while everyone seems to know what economic and social exclusion are in a general sense, the exact meaning in policy analysis and discussion is not always clear. However, three recurring elements permeate the discussions and analyses of inclusion and exclusion (Atkinson, 1998):

1. Relativity: Individuals are included or excluded relative to a given society, a place, an institution. Thus, when one seeks to assess the inclusion of an individual, she must look beyond the individual to the beliefs and behaviors of others with whom the individual interacts.

2. Agency: The act or state of inclusion or exclusion comes to an individual through the acts of agents. For example, an insurer (the principal) may act inclusively or exclusively towards insurees (the agents) of different genders, races, or jurisdictions. Alternately, a university may discriminate (and thereby include and exclude) potential students based on prior academic performance. We may even think of this agency relation as being intra-personal: An individual may exclude herself from the labor market by leaving the labor force. Such exclusion may be self-imposed if the individual withdraws due to pessimism about her earning potential in the labor market.

3. Dynamics: Individuals are not excluded solely because of their current state of welfare, but but because they have limited prospects for the future. An unemployed individual may be included if she believes she has a good chance of once again obtaining gainful employment. On the other hand, an individual who is unemployed and perceives herself as having few opportunities in the labor market may be excluded. As Atkinson (1998, p. 14) argues "Social exclusion is not only a matter of ex post trajectories but also of ex ante expectations."

Thus, definitions of inclusion (and exclusion) are general, focusing on (i) the access to rights and resources and (ii) the presence of obstacles to social institutions without directly defining the rights or institutions in question. Avramov (2002) characterizes social exclusion as

> a condition of deprivation, that is manifested through the generalized disadvantages facing individuals of social groups due to accumulated social handicaps. It is experienced by people as the overlapping of objective deprivation with their subjective dissatisfaction with life chances due to inadequate means and limited access or poor participation in several of the most important domains of human activity... Exclusion is as a rule associated with social stigmatization, blame and isolation, which translated to low self-esteem, a feeling of not belonging and not having been given a chance to be included in society.
>
> Exclusion as a social process is the denial of access to opportunity and social rights to particular individuals or groups of individuals. Social inclusion as positive praxis, on the other hand, is the process of opportunity enhancement for building or re-establishing social bonds by facilitating the access of all citizens to social activity, income, public institutions, social protection and programs and services for assistance and care.
>
> Avramov, 2002, p. 26–7

Note that in the criteria set out by Atkinson (1998), Atkinson et al. (2004) and Avramov (2002) there appears an important role for individuals' beliefs and perceptions (e.g. dissatisfaction, self-esteem) in the determination of inclusion and exclusion.

A notable exception to the lack of definitions is the work of Dayton-Johnson (2003) and Lippert and Spagnolo (2005). Paraphrasing Dayton-Johnson (2003), social capital and social cohesion are defined as follows:

Definition 1 SOCIAL CAPITAL *is an individual's sacrifices (time, effort, consumption) made in an effort to promote cooperation with others.*

Definition 2 SOCIAL COHESION *is a characteristic of society which depends on the accumulated social capital.*

Social capital in the model of Dayton-Johnson (2003) is the flow of individuals' investment. (This approach mirrors than in Glaeser et al., 2002). On the other hand, social cohesion is the stock of these investments which provide individual and social benefits (i.e. externalities). Thus, social cohesion is a characteristic of an economy which affects the incentives to invest in social capital. While this has been defined in terms of the number of mutual dyadic ties between individuals (Moreno and Jennings, 1937) and the field forces acting on members of a group (Festinger, 1950), Friedkin (2004) suggests that

> (g)roups are cohesive when they possess group level structural conditions that produce positive membership attitudes and behaviors and when group members' interpersonal interactions maintain these group level structural conditions. (Friedkin, 2004, p. 421)

Social cohesion is therefore a condition of a group or an economy and as such affects the decision environment faced by the population. Since we think of investments and social capital as requiring trust (Arrow, 1972; Hardin, 2002), social cohesion affects investment decisions by characterizing the extent to which, say, others in the economy have attitudes favoring trust and trustworthiness. Simply put, social cohesion determines how an economy "hangs together" (Maloutas and Pantelidou, 2004). In this way social cohesion affects the incentives to invest in social capital by increasing the return to these investments and reducing the associated uncertainty.

Note that the definition of social capital given above is quite distinct from that utilized in the research of Putnam (2000) and others in which social capital (like physical or human capital) is a stock which is an accumulation of individuals' investments in community, etc. A possible reconciliation of these definitions is to view the combined definitions of social capital and social cohesion in Dayton-Johnson (2003) as making up the definition of social capital in, for example, Putnam (2000): In the latter, social capital is both the stock and the flow of "community" which exists in an economy.

In line with these ideas, we present the following definition of social inclusion. In this definition we focus on the perceptual aspects of inclusion, implying inclusion can be affected by policies and (at the same time) be influenced by decision-making.

Definition 3 INCLUSION *is an aspect of how one perceives her access to institutions and resources in the decision making environment. As such, inclusion affects the way individuals perceive the returns of investing in various forms of capital (e.g. human and social).*

As such, we focus on inclusion as a more personal aspect of an individual's decision making (recall the role of subjective dissatisfaction in the definition of Atkinson, 1998; Avramov, 2002). Inclusion affects the incentives an individual faces when choosing to invest in social capital or behave in a reciprocal manner (as a high level of social cohesion would imply). Inclusion thereby affects not only an individual's access to institutions (as "promoting an inclusionary economy" would imply) but also the beliefs and attitudes an individual holds regarding her access to institutions and the expected returns (through optimism or pessimism) to investments in social capital. Hence, we can conceptualize inclusion in two ways: First, inclusion affects one's beliefs (and perceived incentives) regarding the success of investments and social capital. Secondly, inclusion affects the constraints and resources an individual faces in decision-making by affecting her bleifs regarding access to institutions (e.g., financial, educational, etc.).

Defining inclusion as a perceptual aspect does not suggest it cannot be measured. The behavioral outcomes of inclusion/exclusion are observable and numerous studies have provided measures of inclusion. Moreover, there exist research addressing how inclusion should be incorporated into policy analysis and debate (see Council of Europe, 2001, and the ensuing volumes). Further, defining inclusion as a perceptual component does not imply that inclusion and exclusion are "in one's head." Individuals may be directly excluded via discrimination in the labor market or the inability to acquire certain goods. Alternately, individuals may feel excluded based on their ability to participate in social, political or economic institutions or based on the efficacy of their interactions with these institutions. This follows previous research (e.g. Friedkin, 2004; Oxoby, 2001, 2004) emphasizing the importance of understanding the interrelations between individuals' attitudes and behaviors in developing a coherent framework for understanding social cohesion and investments in social capital. The power in defining inclusion in this manner is that it allows us to make the distinction between weak and strong inclusionary policies (Luxton, 2002). Proactive policy (is aimed at, say, eliminating discrimination) directly affects individuals' perceptions of society, and hence the manner in which they construe inclusion. Alternately, broad-based commitments to equality or reform lacking detail are perceived as vague and unenforceable. Such policies do little to increase individuals' beliefs that their society is inclusive.

This points to an important interrelation between inclusion and social cohesion. Since greater inclusion positively affects one's incentives to invest in social capital, inclusion is a means of creating greater social cohesion. Thus there is a dynamic relationship between these related concepts: In an inclusive economy individuals have better incentives to invest in social capital, in turn raising the stock of social capital and the level of social cohesion. On the other hand, in exclusionary economies there are only weak incentives to invest in social capital. This results in a low stock of social capital and hence low levels of social cohesion. It is this dynamic relationship which helps us highlight and identify the important role of inclusion (measured in terms of trust or investments in social capital) in economic performance (e.g. Glaeser et al., 2002; Oxoby, 2001; Zak and Knack, 2001).

2.2 Capabilities and Inclusion

One of the clearest articulations of exclusion in terms of poverty has been that of Sen (1985, 1992). Sen stresses the role of relative deprivation in precipitating absolute deprivation (and hence exclusion). For example, in terms of incomes, relative poverty may result in absolute poverty (i.e. exclusion) if one is unable to acquire basic needs or adequately present herself to potential employers and peers. The key to understanding this approach lies in Sen's idea of capabilities. According to Sen (1985), commodities provide the capability to maximize one's welfare. Such a view is presented in Figure 1: Individuals purchase commodities with given characteristics and capabilities (e.g. a bicycle has the characteristic of transportation which gives a person the capability to travel to and from work). It is these capabilities that result in economic outcomes (utility).

In the context of previous research emphasizing poverty and exclusion, note that the in-

$$\text{Commodities} \longrightarrow \text{Characteristics} \longrightarrow \text{Capabilities} \longrightarrow \text{Utility}$$

Figure 1: Sen's view of commodities and capabilities (Sen, 1985).

ability to obtain commodities (due to poverty or market imperfections) necessarily reduces an individual's capability to effectively participate in society. This approach has been taken by some to develop more formal and reliable ways of measuring and understanding poverty and development (Brady, 2003; McNeil and Woodcock, 2004). Also note that the idea of increasing an individual's access to capabilities is closely tied to the ideas of equality of opportunity (Roemer, 1998, 2002) and stakeholder society (Ackerman and Alstott, 1998; Wills, 1998). Through a lens of economic inclusion, equality of opportunity implies that all individuals have equal access to the institutions and publicly provided resources which allow them to obtain capabilities and attain their potential. A stakeholder society implies that people have the incentives to use these resources and act in a manner that is inclusive to others.[4]

Figure 2 proposes an expansion of Sen's model to explicitly account for the effects of endowments (which may result in poverty) and policies (which may result in alienation) on inclusion and exclusion. Moreover, the model includes the prospect that individuals' inclusion is a function of their cognitive or attitudinal disposition towards their environment. For example, in economies where the distribution of income is highly unequal, a large portion of the population lives in poverty. This poverty may itself lead to exclusion (as individuals are unable to purchase goods) but may also result in cognitive adaptations which diminish welfare. For example, crime and drug use can develop into behavioral norms as people adapt to living in poverty (Kelso, 1994; Lafree, 1998; Schwartz, 1991). Alternately, policies that are imposed on individuals and which conflict significantly with their preferred policy may result in alienation and hamper the effectiveness of the policy (James and Gutkind, 1985).

[4] Oxoby (2004) uses a model of cognitive adaptation to address the role of stakeholder policies in reducing the size of the underclass. In terms of research on equality of opportunity, Schuetz et al. (2005) analyzes the role of equality of opportunity education policies and Llavador and Roemer (2001) address the allocation of international aid as an incentive for countries to adopt opportunity-based policies.

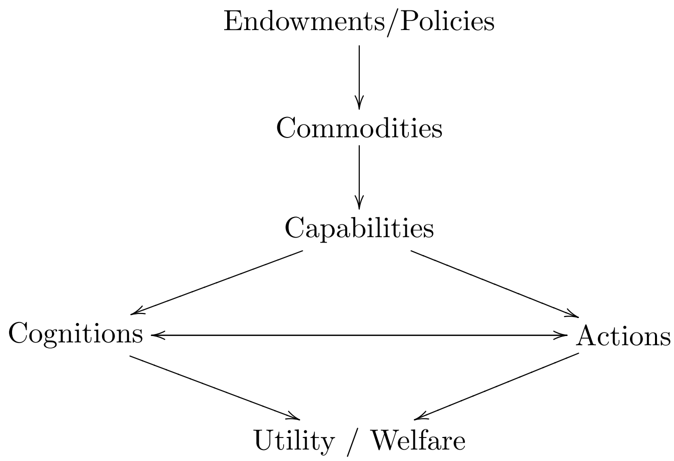

Figure 2: View of capabilities and inclusion presented in the models.

2.3 Policy Approaches to Exclusion and Cohesion

The Council of Europe's Human Dignity and Social Exclusion Project (HDSE, Council of Europe, 2001) characterized two processes as contributing to economic and social exclusion. First, for individuals who were previously integrated in social institutions, high unemployment and "job precariousness" increases the potential for exclusion. Secondly, particularly among younger individuals, difficulty entering the workforce and lack of access to income and associated social networks (i.e. social deprivation) leads to social exclusion. The combination of these two processes creates "the spiral of cumulative disadvantage" which, over time, results in exclusion.

While the HDSE conceptualization of exclusion is not precisely defined, the Council or Europe adopted a perspective in which access to "social rights" became the basis for analyzing and addressing social exclusion (thereby fostering social cohesion). In identifying these rights, the HDSE distinguished among five policy areas.

1. Access to employment: Generally speaking, policies should seek to bring individuals into the workforce by facilitating and enhancing their interactions in the labor market. Policies in this area focus on developing equal opportunity policies (eliminating discrimination) and assisting with the balancing of professional and family responsibilities during

reintegration in the work force.

2. Access to housing: Policies in this area (focusing on urban planning) seek to increase access to and maintenance of housing for disadvantaged groups. In addition, policies focus on responding to short-term and longer-term housing crises.

3. Access to social protection: The removal of obstacles to obtaining social services and benefits has become an essential part of Europe's social cohesion initiative. Policies in this area focus not only on the demand side for these benefits, but also on the supply side by looking to improve the management and partnerships between distribution agencies and private enterprises.

4. Access to health: The emphasis of these policies has been on the adaptation of limited health resources to specific care needs and the access of disadvantaged groups to these resources. Policies in this area range from preventative to palliative care and have addressed the role of information technologies and the media in the distribution of health care information.

5. Access to education: A dominant view has been that lack of training and education is an important cause of social exclusion. Suggested educational reforms focus on equal access, improved quality and lifelong learning skills, and issues associated with youth participation in education. The goal here has been to increase the extent and access to both formal and informal educational services.

The goal of these policy recommendations has been to reduce poverty and increase individual and social welfare. In the eyes of the Council of Europe (2001), the primary difference between these recommendations and those focusing more directly on poverty is that under the social exclusion program the perspective is a dynamic one, focusing on the opportunities and choices individuals face over the long term. As such, the hope is that the social exclusion focus will do more for addressing the "culture of poverty" and the "underclass" (Auletta, 1982; Kelso, 1994; Schwartz, 1991; Wilson, 1987).

3 Theoretical Research

Relative to theoretic research exploring issues of social capital and cohesion (e.g. Glaeser et al., 2002; Dayton-Johnson, 2003), there is a dearth of microeconomics based research addressing inclusion. Therefore, in this section we review various theories which are largely related to the ideas of inclusion and exclusion.

Two broad ideas that we believe are strongly tied to the ideas of economic and social inclusion are the ideas of identity and attitude formation. With respect to identity, Akerlof and Kranton (2000, 2005) provide the most thorough analysis of identity in economic contexts. In this model one's identity is accompanied by behavioral prescriptions (similar to norms of behavior) which dictate how one should behave in social situations. These behavioral prescriptions not only affect a decision maker's behavior, but also create utility and disutility for individuals who share an identity with the decision maker. Thus, if an individual violates the prescriptions associated with her identity, there are externalities which create disutility for individuals of the same identity (e.g. identity threat). Individuals who experience this externality may respond by changing their identity or acting out to reassert their identity.

In terms of inclusion, identity plays two broad roles. First, individuals who share an identity (and abide by the same behavioral prescriptions) view one another as "included" in the identifiable group. This facilitates the presence of "theory of mind" among individuals who identify with one another, thereby facilitating strategic and cooperative interactions (as in Eckel and Grossman, 2005). As a result, individuals who identify with with one another (in the absence of any identity threat) feel a bond of inclusiveness with one another. However, the violation of behavioral prescriptions may result in negative responses from others (as in McLeish and Oxoby, 2006). As a result the inclusiveness created by identity is sharply tempered by identity threat and the abandonment of behavioral prescriptions. This leads us to the second important aspect of identity: Identities (as structural concepts) are inherently exclusive, emphasizing a level of behavioral conformity and distinguishing in-group members from out-group members. This level of exclusion may preclude some individuals from obtaining resources or access to institutions, effectively creating discriminatory practices.[5] In response to this exclusion, individuals may substitute towards other ways of expressing their identity.[6]

From the perspective of social and economic policy, developing a common identity among citizens (e.g. a Canadian identity) will help foster a greater sense inclusion among the population. Note however that developing such an identity necessarily requires differentiating one group (e.g. Canadians) from another (e.g. U.S. citizens). Thus, policymakers must balance the inclusion created by and the exclusion necessary for developing identity. Managing this exclusion requires special attention: Just as one's identity is accompanied by behavioral prescriptions, one's identity also is accompanied by stereotypes and beliefs about those of different identities. Thus developing an inclusive economy requires attention to how policies foster identity and influence of beliefs about oneself and others (see Coate and Loury, 1993; Steele and Aronson, 1995).[7]

A second approach to explaining inclusion and exclusion has focused on individuals' cognitive processes. Much of this work has been used to address issues of poverty, emphasizing the role of the theory of cognitive dissonance (Aronson, 1992; Festinger, 1957) in the formation of attitudes. For example Montgomery (1994) and Oxoby (2003, 2004) develop microeconomic models exploring how individuals who live in poverty (defined as low income) may choose to abdicate mainstream social norms due to the dissonance created by their inability to satisfy these norms. It is this abandonment which results in the behaviors associated with the underclass (e.g. welfare dependency, long-term unemployment or nonparticipation, substance abuse, criminal behavior). In these models, an important aspect in the formation of dissonance (and

[5] This idea is related to the work of Becker (1957, 1974) and Becker and Murphy (2000). The idea of discrimination is clearly germane to our understanding of economic exclusion. If one focuses on inclusion as access to trade (e.g. in labor in labor markets), models of imperfect information regarding productivity (i.e. statistical discrimination, see Arrow, 1973; Phelps, 1972; Lundberg and Startz, 1983) posit results in which minority groups may be excluded from trade. Cornell and Welch (1996) extend this type of model, exploring how cultural traits and norms may influence inclusion.

[6] Oswald (1999) documents how consumer behavior (particularly the purchase of certain goods) serves as a means for maintaining identity in a changing society.

[7] Similar arguments are presented in Council of Europe (2003). Fershtman and Gneezy (2001) find experimental evidence supporting discrimination based on perceived group and racial stereotypes. Steele and Aronson (1995) demonstrate how the fear of confirming a negative stereotype associated with one's identity can result in behavioral consequences (i.e. poor performance).

hence dissonance reducing behaviors) are social and economic aggregates which individuals use to judge their current state.

This research helps us identify ways in which social and economic policies may foster feelings of inclusion or exclusion. An important lesson from these models is the recognition that feelings of inclusion or exclusion are strongly based on the manner in which individuals interpret the policies and environment around them. This implies that it may be difficult to create policies that transition individuals from a state of exclusion to one of inclusion, as it may be difficult to undo the psychological effects created by "moments of exclusion" (Becker, 1998). As a result, inclusionary policies work best if they are proactive, stemming exclusionary forces before they create actual exclusion.

Lindbeck and Snower (1998, 2001) present a model of insiders and outsiders (economic agents in the market where some have more privileges than others) which is closely related to the idea of economic inclusion. In this model, the greater privileges of insiders allows them to command a higher surplus or rents at the expense of outsiders. Thus, the inclusion/exclusion cleavage aligns with an individual's status as an insider or an outsider. These divisions often serve as the antecedents to the problems associated with economic exclusion. This line of research has been useful in explaining the behavior of union and nonunion workers, interactions in internal labor markets, and discrimination. In terms of developing inclusive organizations, this research has implications for the manner in which the employee ownership is structured (Wills, 1998) and the establishment of cooperatives (Wells, 1981).

Sheehy (2004) explores the process by which the legal environment of a society can serve to include or exclude different classes of individuals. In such an environment, inclusion depends largely on the manner in which people perceive their interests as tended to by society (more specifically, the courts system). From a policy perspective this raises the distinction between weak and strong means of promoting inclusion. That is, while commitments to end discrimination or poverty are important practices for an inclusive economy to adopt, these are weak means relative to more direct anti-discriminatory and equality of opportunity policies (Luxton, 2002).

In terms of macroeconomic performance, several theories have been developed (supported by evidence) hypothesizing that an inclusionary economy is a more productive economy. Rodrik (2003) argues for the importance of high quality institutions and context-based growth strategies which are tailored to local needs and constraints. This attention to local needs and the emphasis of institutions (including social institutions) hints at the importance of designing growth policies with inclusion (or at least the symptoms of inclusion) in mind.[8] For example, Gradstein and Justman (2002) and Zak and Knack (2001) argue that reducing social distance and increasing trust are important for economic growth. Gradstein and Justman (2002) develop a model in which the public provision of education serves to reduce social distances (which increase inclusion and the shared identity among individuals). This in turn creates a more cohesive economy, yielding greater trust and raising economic growth (Zak and Knack, 2001) and well-being (Helliwell, 2003a,b).[9]

4 Empirical Research

In terms of empirical research focusing on advancing our understanding of social inclusion (and exclusion), a large body of literature has sought to develop measures of social inclusion and exclusion using existing data. For example, Atkinson (2002, and the accompanying articles) describes the process by which the European Union adopted a set of common indicators for social inclusion. While these indicators include items associated with health, income, education, and employment, it is interesting to note that the indicators emphasize the outputs of social processes, rather than the inputs (which may include the facility by which individuals can access economic and social institutions). Table 1 presents the most recent indicators used by the EU (based on the most recent version presented in Atkinson et al., 2004, 2005).[10]

[8]Similar arguments are made by McCracken (2003) who emphasizes that better economic performance improves social cohesion (especially if the gains from growth are shared among all members of society). Empirically, Knack and Keefer (1997) and Temple and Johnson (1998) identify various channels through which improvements in social cohesion and social capital can directly and indirectly affect macroeconomic performance.

[9]Stanley and Smeltzer (2003) cite empirical evidence demonstrating that social cohesion (namely trust and the willingness to cooperate) partially explain economic growth and investment.

[10]Cherchye et al. (2004) develops a conceptual framework for the proper aggregation technique for social inclusion measures. While others (e.g. Atkinson, 2002) have focused on measurement, the focus here is on

Given these indicators, researchers have developed indices which utilize the indicators to rank economies based upon inclusion/exclusion. For example, Bossert et al. (2004) axiomatically characterize a social exclusion index for use in analyzing the European countries.[11] The authors use this index to rank E.U. countries based on their degree of social exclusion (Table 2). Note that Portugal and Greece have the highest degrees of social exclusion, while the Nordic countries (the Netherlands and Denmark) have the lowest degrees of exclusion. With these measurements in place, the next step becomes analyzing the countries, specifically the policies, demographics, and institutions that explain these differences. For example, the stronger social welfare systems in Nordic countries may be evidence of higher social cohesion resulting from lower levels of exclusion.[12] While these countries maintain relatively the same rank whether they are evaluated based on standard measures of income inequality (i.e. the Gini coefficient) or access to institutions (e.g. mean years of education, male/female ratio in primary and secondary school, infant mortality rate), neither of these other measures provide an accurate portrayal of exclusion. This emphasizes the importance of theoretical developments in measuring and defining inclusion and exclusion.

With these measures, a new research agenda has developed exploring how the information gleaned from the indicators can be used in policy analysis. The value of this research has been to explore how an economy can improve inclusion among its population. Given the multi-dimensionality of these indicators, these studies have focused on specific aspects of the inclusion process. For example, McGregor (2000) and Till (2005) explore the role of housing

policy and benchmarking.

[11] The axioms employed by Bossert et al. (2004) include focus (dealing with that individual's functioning rather than her income), conditional anonymity, homogeneity, translation invariance, and population proportionality. Other such approaches include the work of Bourguignon and Chakravarty (2003), Chakaravarty and D'Ambrosio (2003), and Estaban and Ray (1994, 1999).

[12] It is worth noting that the Nordic countries are the most homogeneous of those listed in Table 2. The lower levels of social exclusion may be explained by the arguments of Alesina et al. (2001) and Lee and Roemer (2004): The differences between the U.S. and European welfare states is attributable to racism (perhaps the strongest form of exclusion).

Primary Indicators

1. Low income rate after transfers with low-income threshold set at 60% of median income.
2. Distribution of income (income quintile ratio).
3. Persistence of low income.
4. Median low income gap.
5. Regional cohesion.
6. Long term unemployment rate.
7. People living in jobless households.
8. Early school leavers not in further education or training.
9. Life expectancy at birth.
10. Self perceived health status.

Secondary Indicators

1. Dispersion around the 60% median low income threshold.
2. Low income rate anchored at a point in time.
3. Low income rate before transfers.
4. Distribution of income (Gini coefficient).
5. Persistence of low income (based on 50% of median income).
6. Long term unemployment share.
7. Very long term unemployment rate.
8. Persons with low educational attainment.

Table 1: Primary and Secondary E.U. Indicators for social exclusion (definitions of each available in appendix to Atkinson et al., 2005).

Country	Index I	Index II	Gini Coefficient	Mean Yrs. Education	Ratio F/M in School	Infant Mort. Rate
Belgium	276	78	0.26	11.52	106	8
Denmark	211	53	0.27	11.62	103	8
France	308	98	0.31	8.26	100	7
Greece	560	97	0.36	n.a.	101	10
Ireland	373	43	0.31	11.00	n.a.	8
Italy	372	138	0.31	9.05	98	8
Netherlands	240	51	0.29	12.36	97	7
Portugal	663	153	0.39	n.a.	102	11
Spain	399	97	0.35	9.12	103	8

Table 2: Social exclusion measures for EU countries from Bossert et al. (2004, Table 1). Index I includes the domains of financial difficulties, basic necessities, housing, and durables. Index II includes the domains of health, social contact, and dissatisfaction. Other information from World Bank (2004, 2006).

(including market competitiveness, integration and tenure) through the lens of social inclusion. Given this lens, the focus is not merely on the form of housing (e.g. renting versus owning) but on the interaction between these forms of use/tenure and other factors (including labor market conditions). Other have focused on employment and labor market conditions (Atkinson, 1998), emphasizing the importance of skill requirements and training in the determination of long-term/short-term employment and the identification of low income as a permanent or transitory state. A slightly different approach has been to use the information from the indicators to address and distinguish between community exclusion and national exclusion (Berman and Phillips, 2000; Phillips and Berman, 2003). In this research, the emphasis has been on access to local and national institutions and the role of communities in enhancing social quality and inclusion . Finally, using the indicators and indices as benchmarks, some researchers have sought to provide an integrated approach, addressing issues of health, income and consumption, poverty, labor market and political participation, and social networks in a unified framework (e.g. Buvinic et al., 2004; Gacitua-Mario and Wodon, 2001; Feinstein and Picciotto, 2000). The theme in these studies (notably Buvinic et al., 2004) has been to address the exclusion faced by minorities, those with disabilities, and people with health concerns (in particular HIV/AIDS).

From these studies policy recommendations have been developed regarding anti-discrimination legislation, guaranteed income subsidies, and ethnic/racial political organizations.

Other empirical work has looked more directly at case studies and data in an attempt to understand the dynamic forces and policy implications of inclusion. Adopting a case study methodology, Lareau and Horvat (1999) explore how parents' decisions and involvement in their children's education is affected by their previously experienced "moments" of inclusion and exclusion (e.g. discrimination). Becker (1998) analyzes how two different congregations became racially inclusive following racial changes in their communities. Results indicate that the greater the communal involvement of the church (in terms of greater attention to practical experience than theology) and the more attention the congregation paid to timing (implementing changes once the community had achieved stable racial integration), the less costly and more cohesive was the transition to a racially inclusive community. Relatedly, the macroeconomic practices and economy-wide institutions of a society can influence inclusion among a population. For example Ginsburgh and Weber (2005) argue that maintaining linguistic diversity (i.e. maintaining French and German as working languages in light of widespread knowledge of English) is important for mitigating disenfranchisement and exclusion among European citizens.[13] While most of these studies have focused on the racial, linguistic, and class-based divisions which an inclusive community must overcome, it is important to note that the dimensions of inclusion and exclusion may be as innocuous as individual's musical preferences (Bryson, 1996).

An important point to understand is that inclusion/exclusion is multidimensional. As a result, if individuals are excluded in one dimension of life, they may seek to find inclusion in another area. To this end, Eitle and Eitle (2002) study individuals' decisions regarding sports participation. They find that cultural capital matters significantly in the decisions of black and white youths. One interpretation of this result is that when individuals find themselves

[13]Grafton et al. (2004) analyzes the role of communication barriers in the productivity and capital accumulation. It is interesting to note that during the 1985 to 1996 period of significant European reforms Micklewrigh and Stewart (1999) find that child poverty and the social exclusion of children in the European Union increased. Relatedly, Phipps (2003) find that greater inclusion during childhood (characterized as good relationships with parents and others) are significant in affecting current well-being.

excluded in one area of life (e.g. due poor performance in school) they may seek inclusion in other areas (e.g. athletic teams).[14]

In the economics literature, more attention has been paid to the interrelationship between inclusion and institutions, policies, and outcomes than to the formation or development of inclusion. Hoselitz (1955) was one of the first to address the effect of urban centers and development on social cohesion and economic inclusion, arguing that cities play and important role in the process of cultural change and help establish a "city consciousness" which can foster inclusion. The distinction here is between central cities (which are often older and may hold political or historical importance) and industrial cities (which there is greater in-migration due to employment and higher wages). The difficulty here (particularly in developing nations) is balancing new norms that an industrial city requires against more traditional (and potentially more exclusionary) forms of social behavior which come from more rural areas.

Counterbalancing this, the greater heterogeneity in cities may have economic outcomes that are associated with exclusion: Glaeser and Sacerdote (1999) and Alesina and Ferrara (2000) find that crime is higher and participation in social groups lower in urban areas where there is greater heterogeneity and less cohesion. This suggests that the key to developing inclusive urban areas is in managing the diversity that accompanies urbanization. Wacquant and Wilson (1989) argue that the evolution of the underclass (characterized as a structural concept) in urban areas is largely due to the economic marginalization of racial and economic groups. It is this marginalization which results in long-term joblessness, economic exclusion, and ghettoization. The latter creates additional cleavages among social classes which create exclusion not only through the choices of the individuals in question but also through a lack of incentives for employers to create jobs in these areas (Wilson, 1987, 1989).[15]

Political institutions can also play an important role in developing or quashing inclusion. In the simplest of cases, the right to political participation and the ability to express one's po-

[14] It is important to note that seeking inclusion in other areas (e.g. athletics) may have detrimental effects for performance in other areas (e.g. academics). See Eitle and Eitle (2002).

[15] Hoffman (2003) argues that policies promoting tourism may serve as a means for increasing inclusion in impoverished areas.

litical voice are key elements of promoting an inclusionary economy (Council of Europe, 2001). Moreover, the distribution of political voice can have significant effects on economic outcomes (Acemoglu and Robinson, 2000; Lizzeri and Persico, 2004; Llavador and Oxoby, 2005). This implies that democratization can be favorable to social inclusion by demonstrating to individuals that their opinions and preferences matter in charting the direction of an economy and policy design. It is therefore not surprising that democratization often follows, and is positively correlated with, economic development (Huber et al., 1993; Llavador and Oxoby, 2005; Schwartzman, 1998): The presence of rapid economic change may create exclusionary forces which are balanced by political inclusion.[16] That said, it is important to recognize that the structure of changes in the suffrage and the costs associated with expressing one's political voice may lead to exclusion.[17]

Finally, there is a large empirical literature documenting the positive benefits of inclusion (and its related concepts) on health outcomes. In addition to empirical investigations by the Council of Europe (discussed in Avramov, 2002; Council of Europe, 2001), Lavis and Stoddart (2003) use the World Values Surveys to address the relationship between trust and self-reported health status. The authors find the trust is positively associated with good health in many developed countries. This suggests a greater social inclusion (be it by the psychological state inclusion induces or the increased opportunities for income and access to institutions inclusion provides) is significantly related to better health outcomes.

5 Conclusion

In this paper, we have tried to highlight the important issues and causal directions in promoting an inclusionary economy. In addition to reviewing the existing literature on economic and

[16] Lokshin and Yemtsov (1999) empirically documents how social exclusion increased during the crises in Russia. To the authors also address the strategies used to cope with these crises.

[17] Collier (1999) explains how "voluntary registration" in the United States (in which individuals had to register in specified places prior to each election) effectively disenfranchised millions of individuals. Similarly, Lord Sydenham use the location of polling places in the timing of elections to effectively disenfranchise many French-Canadians (Abella, 1966). These practices reduce political efficacy and (perhaps subtly) exclude individuals from political participation.

social inclusion, we have presented three models of individual behavior focusing on the way inclusion and exclusion are manifested and mitigated by economic policies. An important point these models raise is that there exist trade-offs between inclusion and economic efficiency. Perhaps more importantly, there exist trade-offs between promoting inclusion with respect to one group and creating exclusion with respect to another. Effective policymaking in the realm of economic inclusion therefore requires careful attention to the opportunity costs and trade-offs of implementing various policies.

Casual empiricism tells us that there are significant benefits to living in a inclusionary economy than one that is exclusionary. The task facing researchers and policymakers is identifying the causal elements of inclusion and developing policies that promote an inclusionary economy.

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