

Chapter 6

Social Capital, the Culture of Trust, and Economic Development

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ABSTRACT

The benefits accruing from social networks and structures have been shown to correlate with economic performance at both the macro- and micro-levels. Indeed, social capital can be seen as a catalyst through which human and physical capital are utilized and political and economic freedom realized. In this chapter, the authors briefly review the broad extant literature on social capital before embarking in more detail on how game theory can be used to analyze and model social capital. Particular attention is given to the population game approach. This approach is well suited to model social capital as it allows us to capture individual behaviour, societal influence, and network structure. The growth of social capital is seen to depend on the incentives for cooperation, the way in which people learn from past experience, and the inter-connectedness of the social network. A particularly important question for many emerging economies is how social capital can be encouraged to grow from a low base. In a concluding section, which includes a discussion of the complementarities between strong institutions and social capital, the authors use the population game approach to study this issue.

1. INTRODUCTION

During the past 20 years a burgeoning interest has developed in social capital and an increased recognition that it has a fundamental role to play in economic development. In this chapter we shall introduce the literature on social capital, and discuss the importance of social capital in

emerging markets. In broad terms, social capital measures the benefits which accrue from social networks and social structures. A widely cited definition is available from Pierre Bourdieu (Sobel 2002: p. 139): “Social capital is an attribute of an individual in a social context. One can acquire social capital through purposeful actions and can transform social capital into conventional economic gains. The ability to do so, however,

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depends on the nature of the social obligations, connections, and networks available to you”. This definition highlights the crucial, dual nature of social capital – something which is acquired by an individual but can only be realized through the connections this individual has with others.

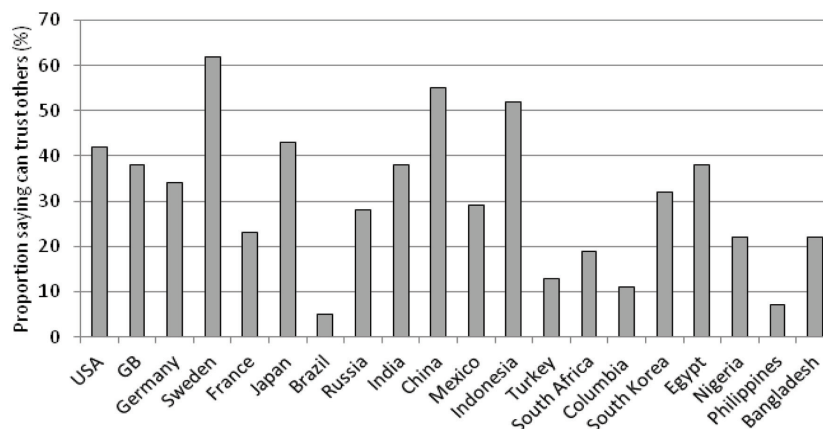
To put this definition in context, consider an economic exchange between two people; for example, consider someone buying a good from another. This exchange will only take place if both buyer and seller have trust in each other. The buyer needs to trust that the seller will supply the good as promised. The seller needs to trust that the buyer will pay for the good as promised. Both seller and buyer need to trust that the legal system (or otherwise) will protect them in case the other side reneges on the deal. The exchange is unlikely to occur without such trust. Therefore, the lack of trust is a potentially large source of economic inefficiency. To quote Nobel Prize recipient, Kenneth Arrow (1972), “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.”

Let us now fit the example of economic exchange within the context of social capital.

Suppose the buyer is willing to trust the seller and that the buyer will honor his promise to pay for the good due to internalized social norms or norms of reciprocity. In this instance, the seller possesses social capital because she can perform the exchange without fear of loss. The crucial thing to highlight here is that social capital accrues to the seller because the seller benefits from the buyer’s trust and honesty. Similarly, social capital accrues to the buyer if the buyer benefits from the seller’s trust and honesty. Therefore, social capital is acquired by an individual, but can only be acquired through the connections available to that individual.

We see in the context of economic exchange that social capital can come in different forms – trust, honesty, reciprocity, norms. Measuring such things is not easy (Glaeser et al. 2000, Fehr 2009). However, the clear consensus one receives is that social capital varies enormously from country to country. Moreover, social capital is lacking in many emerging and developing countries. To look at trust for example, there is now strong evidence of stark cross-country variation in average trust (Rothstein & Uslaner, 2005; Zak & Knack, 2001). To illustrate, Figure 1 compares one measure of trust across a selection of developed and emerging economies.

Figure 1. The proportion of respondents who said ‘most people can be trusted’. Aggregate data from the 1981 to 2000 World Value Surveys.



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