



Tom Connor's Thinking Forward:

Trust Matters

Synonyms: *trust, faith, confidence, reliance, dependence*

Trust has only recently become an area of interest to economists. Traditional views of economic growth have analyzed physical and financial inputs of production: the labor force and its capabilities, capital and the financial resources to instigate and sustain investment, market size and protection, and foreign exchange, amongst others. The role of institutions has often been included to the extent they affect allocations of these inputs.

The inclusion of trust as an issue reflects a transition in economic constructs. For several decades during and after the 1930's, economic theory reflected the mathematical precision consistent with rational, deterministic models. The approach verified economic efficiency, but the assumptions about the decision making process have not all been supported by recent contributions from neuroscience. Social and other institutional environments have an impact on choices and decision-making, and are important to include.

Close upon this has been increased concern about declining levels of trust worldwide. At its 2003 annual meeting the World Economic Forum made trust its theme. The Forum, an independent organization of world leaders in business, government and academics, is committed to developing partnerships among these leaders to help shape global, regional and industry agendas. Using a global public opinion poll, conducted bi-annually since January 2001 by GlobeScan Incorporated, the group monitors the level of trust among countries and institutions. Before the 2006 meeting Doug Miller, President of GlobeScan offered his perspective on the observed decline in trust worldwide:

"...these poll results suggest we're in danger of becoming unstuck – especially when values-driven organizations like non-governmental organizations (NGOs) and the United Nations are losing trust almost as quickly as large companies. It's time for all organizations to better understand how to earn the public's trust."¹

In their 2001 article published in the *Economic Journal*, *Trust and Growth*², Paul J. Zak and Steven Knack, analyzed the role of trust, and its importance in economic growth across countries. Their assumption is that people recognize different levels of trust and compensate when trust is low by investing resources to acquire more information to verify the agent/broker's fealty.

¹ - Full Survey: Trust in Governments, Corporations and Global Institutions Continues to Decline; <http://www.weforum.org/site/homepublic.nsf/Content/Full+Survey:+Trust+in+Governments,+Corporations+and+Global+Institutions+Continues+to+Decline>

² - <http://www.pauljzak.com/pdf/Trust> and Growth.pdf Paul J. Zak and Stephen Knack, *The Economic Journal* 111:295-321, 2001

"We show that trust depends on the social, economic and institutional environments in which transactions occur. Because trust reduces the cost of transactions (ie less time is spent investigating one's broker), high trust societies produce more output than low trust societies."³

Trust Games

Recent experiments among neuroscientists also help focus attention on limitations of the rational, economic model. An experiment, called the Trust Game, tests the self-interest of players, and establishes that at least under some circumstances, people reduce their self-interest, and display trust and willingness to cooperate with others.

The experiment pairs anonymous players and initiates a potential exchange. Each player receives a sum of money (\$10.00). Instructions are that Player 1 can send a sum between \$0 and \$10 to player 2, and that player 2 will receive 3 times the amount sent. Then, the second player may send an amount back to player 1, and that amount can be anywhere between \$0 and \$40. There is no second round and players know that.

In traditional simulations, players are assumed rational, economic people who maximize their self-interest, and player 1 would realize player 2 would send nothing back so player 1 sends nothing. However, in one implementation of the game first players sent over \$5 to the second player, and one third of the second players sent back more than was sent them.

"On average Decision Maker1's send over \$5 and roughly one third of the Decision Maker2's reciprocated by sending back more than was originally sent even though the double-blind condition implied no one would know what Decision Maker2 really did. During sets of this game, it is common that up to one-half of the first players chose to trust the second player. The consensus is that both players recognize that the total amount between them is larger with cooperation. The rational, economic man argument keeps the minimum, but the social, trusting participants realize those constraints and share trust, and a larger financial pie."⁴

Relationships

Relationships are between people, whether the people represent businesses, other institutions, or themselves, and trust is an important part of the development of these relationships. Most of the time we're used to interpersonal contact to help develop our response to others, and very often it's the subtleties of the messages sent and received that can be most influential. These are critical to the development of relationships, but not easily quantifiable.

They also require time. Most non-business relationships start with personal interaction, although that may not be the case with all relationships. However, businesses have long recognized the importance of inter-personal interactions. Face-to-face meetings, social events and other contacts that help people establish relationships have always been important to develop relationships of trust and confidence.

³Ibid, p 296

⁴ - Trust Games; http://neuroeconomics.typepad.com/neuroeconomics/2003/09/trust_games.html

The arrival of the Internet and Online technologies, however, is different. Business transactions take place online without two people necessarily communicating directly. Issues of security and confidentiality are technical and important to develop the trust necessary, and some online business communities provide feedback methods so potential participants can evaluate reliability and reputation of participants, usually the sellers, but that's not enough.

Despite the lack of interpersonal contact, the Internet has become one of our most common means of communication. The Pew Internet and American Life Project summarize it by quoting one of their experts: "I never would have expected that such a high percentage of people would be utterly dependent upon the internet for such a large proportion of their daily communication activities. If you took it away, we would be shell-shocked. But ten years ago, we didn't even have it."⁵

Forrester Research has estimated 2005 online retail sales at \$165 billion.⁶ This is a 20% increase over 2004 and represents a 23% increase in holiday sales. While general economic conditions (rising energy costs among them) create a relative advantage for online business – online businesses need to recognize the full dimension of the developing relationship, and the special nature of online communication in that development. It's no less important than when salespeople managed the relationships.

Many industries, including computers, financial services, books, and automobiles have been part of this transformation. In the past, every one depended on a sales force to develop and manage relationships with customers. Today, to one degree or another, all use the Internet for these relationships, some in part, and some completely.

Relationships can be subtle, and they are important to the development of trust. While many online sites address some technical aspects, and provide information on reputation, reliability, etc. as part of their effort to build trust, trust is more.

Both the Organization of Economic Cooperation and Development (OECD) and World Economic Forum, by making trust a central part of their attention are contributing to the recognition of its importance. The OECD is developing plans to measure and report results of levels of trust among member governments of the organization:

"The OECD, meanwhile, plans to step up its efforts to help governments with reform, notably with a new project dubbed "Management in Government: Comparative Country Data". This will bring together data and experience from across the OECD on good government and efficient public services, leading to an annual report by 2009."⁷

The OECD is also giving special attention to the online community:

"Creating an online environment which builds on trust among users of ICT networks is an increasing priority for business, industry and governments and has been on the OECD agenda since the late 1990s. The aim of this report is

⁵ - The Future of the Internet, Pew Internet and American Life Project, January 9, 2005, p. 48

⁶ 2005 US eCommerce: The Year In Review;

<http://www.forrester.com/Research/Document/Excerpt/0.7211.38809.00.html>

⁷ OECD Observer, January 2006,

http://www.oecdobserver.org/news/fullstory.php/aid/1773/Vote_of_confidence.html

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to undertake a review of the data available from official, semi-official and private sources, which can assist in informing developments and progress in this area. There is a need to be able to use relevant data to assess the effectiveness of public and private initiatives aimed at building trust among users.”⁸

For businesses however, trust is no less important. During a plenary session on “Global Business – Saviour or Scapegoat?” at the 2006 World Economic Forum the discussion turned to trust. As quoted by the Forum, Michael E. Porter, Bishop William Lawrence University Professor, Harvard Business School, summarized the role of business:

“Without business we have nothing. Business is a precondition to any healthy society; companies haven't done a good job at building the trust. They have not done a good job at understanding how their impact on communities where they work affects long-term prosperity.”

“Only by working with stakeholders will trust be restored. Companies will have to go farther and show they are doing good for the community and not just the company.”⁹

There are many dimensions to trust. However, relationships in an online environment are just as demanding of trust as those pre Internet. What is different is that the means and methods to develop trust in an online relationship are new to us, and most of us are only beginning to suspect the dimension and tools that help build reliable, trusting online relationships that matter. Those who do it successfully will recognize the benefits that strong relationships bring. Some things just don't change.

We hope you enjoyed Tom Connor's **Thinking Forward** article. To be notified when Tom or our other author's enter an article, please go to <http://www.hungrypeasant.com/remindme.cfm>. You can contact Tom with questions or thoughts about what you've read at tomc@ridma.com.

⁸ http://www.oecd.org/LongAbstract/0,2546,en_2649_34223_35792807_119666_1_1_1,00.html

⁹ Global Business – Saviour or Scapegoat? ;

http://www.weforum.org/site/knowledgenavigator.nsf/Content/_S15369?open&event_id=1462&year_id=20