Honesty and Trust in Economic Relationships

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Biographical Note

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Abstract

Trust is not a homogeneous phenomenon. In economic relationships different trust structures are at work, including distrust, negative trust and lack of trust. Perceived honesty and competence co-determine the trust structures economic agents have in their interactions with others. Trust structures influence the way agents engage in economic relationships. Honesty and competence should be developed to improve trust in economic relationships. Ethics is not a luxury of advanced economies, it is an indispensable means to foster economic development.

Keywords: honesty, competence, trust structure, social categorisations, economic strategies.

Introduction

There is a variety of relationships in which economic agents interact with each other. Business-to-customers, business-to-employees, business-to-business, business-to-government, and business-to-citizens, are the most important relationships in the present-day economy.

In economic relationships different trust structures may emerge. The basic question is not the general trust among economic agents as stressed by Fukuyama and others (Fukuyama, 1995). Economic agents do have *distorted forms* of trust, which turn their relationship into ineffective, dysfunctional or even destructive interactions. Post-socialist economies give a rich illustration of different forms of distorted trust in relationships among business, customers, employees, and government.

Trust Structures

Theoretical and empirical arguments from economics and psychology suggest that honesty and competence co-determine the trust structures economic agents have in their relationships.

In studying the inter-firm relations in Britain and Japan, Mari Sako has distinguished among three major types of trust in economic relationships. She described contractual trust, competence trust and goodwill trust (Sako, 1992).

Trust is described by Sako as a state of mind, an expectation held by an economic agent about another, that the other behaves or responds in a predictable and mutually acceptable manner. The predictability of behaviour exists for different reasons, which allows us to distinguish between different types of trust. The first type of trust is called *"contractual trust"* which is based on the expectation that by written or oral agreements parties upholding a universal ethical standard, keeping promises. A second type of trust concerns expecting a partner performing its role competently. Such trust is called *"competence trust."* A third type of trust refers to expectations of open commitment to each other. This trust in open commitment is labeled *"goodwill trust."*

Psychologist Gian-Vittorio Caprara and his colleagues studied "brand personalities," i.e. features by which people perceive and evaluate brands. Using the famous "Big Five" model of personality psychology they found that two major factors are at work in people's perception of brands (Caprara, G-V et al., 2001).

The Big Five Model reduces the adjectives describing human personalities to five dimensions (extroversion, agreeableness, conscientiousness, emotional stability, and openness). This framework classifies and organises descriptors of human personality. Caprara and his colleagues studied 12 mass-market brands. Their results show that the five-factor structure is not reproduced when describing brands. Their data support a two-trait solution at a higher-level abstraction in the hierarchical organisation of personality characteristics. One factor shows aspects of brands linked to *stability, predictability*, and *pleasantness.* The other factor shows aspects of brands linked to *dynamism, activity*, and *innovation*.

Based on the above reported results from economics and psychology a model can be developed in which the perceived honesty and competence co-determine trust agents develop in their economic interactions (see Table 1).

Different combinations of perceived honesty and competence give the following categories:

(α) high-level honesty and high-level competence generate *trust;*

(β) low-level honesty and high-level competence generate *negative trust*;

(γ) high-level honesty and low-level competence generate *distrust*;

(δ) low-level honesty and low-level competence generate *lack of trust.*

Trust structures (α),…(δ) induce different social categorisations. In the case of trust others might be characterised as *"good guys."* In the case of negative trust others might be characterised as *"gangsters."* In the case of distrust others might be characterised as *"impotents."* In the case of lack of trust others might be characterised as *"underdogs."* (see Table 2).

Table 1: Trust Structures		
Competence **Honesty**	High	Low
High	**trust**	**distrust**
Low	**negative trust**	**lack of trust**

Table 2: Social Categorisation of Others		
Competence **Honest**	High	Low
High	**"good guys"**	**"impotents"**
Low	**"gangsters"**	**"underdogs"**

An Empirical Study of Trust Structures

In 2002 I conducted a pilot empirical study about the perceived competence and honesty of control organisations operating in the Hungarian economy. *Control organisations* are those parties, which belong to the control sphere of the economy and aim to control the behaviour of economic agents (Kornai, 1971).

I asked 100 graduate students of the Budapest University of Economic Sciences to reveal their perception of honesty and competence of the following control organisations of the Hungarian economy: Hungarian Financial Supervisory Authority, Hungarian Advertising Association, Tax and Financial Control Administration, Environmental Protection Authorities, Association of Hungarian Trade Unions, Hungarian Competition Authority, National Chamber of Commerce, and Consumer Protection Authority.

Students evaluated the control organisations in the dimensions of honesty and competence separately. In both cases students were asked to use a scale of 1-5 where "1" meant the lowest performance while "5" meant the highest performance. Students have had some professional knowledge about the control organisations under study and have had some business experiences.

Table 3: Honesty and Competence of Hungarian Control Institutions				
	Honesty (1-5)	**Competence (1-5)**	**Interpretation**	**Possible Social Categorisation**
Hungarian Financial Supervisory Authority	3,63	3,75	Honest and competent	"good guys"

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Hungarian Advertising Association	3,61	3,87	Honest and competent	"good guys"
Tax and Financial Control Administration	2,83	3,32	Partly dishonest but partly competent	"gangsters"
Environmental Protection Authorities	3,71	2,88	Honest but partly incompetent	"impotents"
Association of Hungarian Trade Unions	3,01	2,89	Partly honest and partly incompetent	"impotents"
Hungarian Competition Authority	3,72	3,85	Partly honest and partly competent	"good guys"
National Chamber of Commerce	3,45	3,45	Partly honest and partly competent	"good guys"
Consumer Protection Authority	3,01	3,24	Partly honest and partly competent	"good guys"

The reported result suggests that students display trust toward the Hungarian Financial Supervisory Authority, the Hungarian Advertising Association, and the Hungarian Competition Authority and to less extent also towards the National Chamber of Commerce and the Consumer Protection Authority. They display *distrust* toward the Environmental Protection Authorities and the Association of Hungarian Trade Unions. They display *negative trust* toward the Tax and Financial Control Administration.

Policy Implications

Trust structures and the corresponding social categorisations are important because they influence the ways economic agents engage in relationships with others. If agents categorise others as "good guys" then they tend to *invest* in the relationships with others. If agents categorise others as "gangsters" then they tend to *avoid* relationships with others. If agents categorise others as "impotent" then they tend to *reduce* their relationships with others. If agents categorise others as "underdogs" then they tend to exploit their relationship with others (see Table 4).

It is not easy to transform distorted trust structures into trust. Agents should be perceived as competent and honest to be recognised as trustworthy. Instruments of *business* and *professional ethics* can help economic agents for developing their honesty and competence profile. Major means include training programmes by professional associations, developing business ethics institutions in organizations, and initiating stakeholder dialogues.

Table 4: Strategies in Economic Relationships		
Competence **Honest**	High	Low
High	**invest**	**reduce**
Low	**avoid**	**exploit**

There are different ways to transform "gangsters," "impotents" and "underdogs" into "good guys." Professional associations can help to improve the competence of agents categorised as "impotents" and "underdogs." Techniques of business ethics and stakeholder dialogue can contribute to develop the honesty of agents categorised as "underdogs" and "gangsters."

Avoiding, reducing and exploiting strategies produce enormous transaction costs and result in great opportunity losses in the economy. Therefore, distorted trust structures considerably reduce economic efficiency. *Ethics* is not a luxury of advanced economies. Rather, it is an indispensable means, which *fosters economic development*.

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