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Love thy neighbor? Recessions and interpersonal trust in Latin America

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ABSTRACT

Trust is critical during times of institutional crisis, but intuition is ambiguous with regards to economic calamity: would a scarcer supply of goods cause greater animosity, or does a worsening economic climate constitute a common foe against which people can unite? This study investigates the relationship between the experience of recent recessionary years and levels of interpersonal trust, specifically in Latin America. First, we find that as the number of recessionary years grows larger, the strength of interpersonal trust increases; the results are generally robust to the effects of time and alternate measurements of recession. Second, levels of trust are positively correlated with confidence in the central government but negatively with corruption, robust to political ideology. Finally, we refute the assertion that Catholicism hinders economic growth through strong vertical trust channels. Instead, we find that religiosity, especially Catholicism, increases levels of interpersonal trust. Understanding such relationships opens doors for policy tools which can utilize strong central government or community-level efforts without sacrificing levels of trust in the alternate measure, in addition to options which take a hybrid approach.

1. Introduction

Trust is critical during times of institutional crisis (McKnight and Chervany, 1996; Mishra, 1996; Webb, 1996; Weick and Roberts, 1993). However, there is a lack of empirical literature discussing the role of trust during and following periods of economic crisis. Intuition is ambiguous: would a scarcer supply of goods cause greater animosity, or does a worsening economic situation constitute a common foe against which people can unite?

Trust is especially important in the Latin American context in reference to a longstanding discussion in the literature regarding “horizontal” and “vertical” sources of trust. Horizontal trust refers to the interpersonal relationships among peers, whereas vertical trust refers to the degree of confidence and trustworthiness one feels toward their institutions, superiors, or elected officials (Eek and Rothstein, 2005; Newton, 1997; Scholz and Lubell, 1998). The sweep of political change across Latin America during the last three decades has often confounded this potential dichotomy by, for example, electing politicians with both strong authoritarian (vertical) and populist (horizontal) platforms. When someone votes for Hugo Chavez, a strong central authority with populist policies, are they doing so because they feel he is one of their peers, or because they admire his ability as a superior? Does a gain in one trust channel come at the expense of the other? And how would this change if the economy was in a recession? Over the last 30 years, Latin America has evolved from a region of remarkable monetary, fiscal, and political volatility to one of relative stability (Daniel, 2009; Solimano and Soto, 2005, p.5; Gavin et al., 1996). Since this

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trend toward stability occurs despite growing disparities in income and political ideologies, exploration of unconventional channels of social, economic, and political interaction is warranted.

This study investigates the relationship between recent experiences of national recessions and levels of interpersonal trust, specifically in Latin America. Using probit analysis, we explore the links between trust, recessions, and a wide variety of experiences and beliefs during each of four waves of the World Values Survey, an established and comprehensive survey of social, political, and cultural indicators. This analysis yields several important insights. First, we find that as the number of recessionary years grows larger, the strength of interpersonal trust increases. Second, levels of trust are positively correlated with confidence in the central government, robust to political ideology; further, results are relatively robust to the effects of time and alternate measurements of recession. Finally, we do not find support that Catholicism discourages interpersonal trust as suggested in the literature, providing another example of the positive correlation between horizontal and vertical trust channels. Policy implications for using trust channels during times of economic stress are discussed.

2. Foundations

2.1. The link between trust and economic growth

Trust has long been recognized as an essential component of civil society (Almond and Verba, 1963; Arrow, 1974; Sztompka, 1999; Fukuyama, 1995; Coleman, 1988, 1990). In economic literature, studies of trust have concentrated on its role in economic growth using two potential theories: property rights and transactions costs. Expectations of mutual respect and reciprocity must exist for property rights, even before such norms are reinforced by a community (Berg et al., 1994; Kandori, 1992); without an acknowledgment of property, there is no incentive to invest and grow. Alternatively, the existence of trust between individual or institutional actors reduces the amount of fact-finding that one must regarding history of a potential economic partner, thus reducing transactions costs and facilitating economic activity (Zaheer et al., 1998; North, 1990). In the 1990's, these two areas of analysis fused to explicitly study the relationship between trust and economic growth. Zak and Knack (2001) document the existence of the "low trust poverty trap" which arises from a reluctance of societies with low levels of trust to invest; a 15% increase in the percentage of citizens answering positively to the same indicator used in this study is associated with a 1% increase in economic growth. Similarly, Knack and Keefer (1997) find that interpersonal trust bolsters economic growth, though primarily in countries where few reliable formal institutions exist. This study differs from the previous literature, however, in three ways. First, all of these areas of analysis restrict trust to the status on an independent variable (Zak and Knack, 2001); though we do not claim clear causality, the construction of multiple time-based measurements of recession are designed to measure the impact of recessions on trust rather than vice versa. Second, few trust studies have been made of Latin America specifically – Knack and Keefer (1997), Zak and Knack (2001), and Beugelsdijk et al. (2004) all use an assortment of countries from around the world; Easterly and Levine focus on Africa (1997). Finally, many of these studies utilize other covariates, especially ones relating to investment rates and types. The most similar of these studies to the one at hand, Dearmon and Grier (2009), uses not only the World Values Survey, but also the World Development Indicators and Barro datasets which this study uses. However, their choice of dependent variable, lack of regional focus, and inclusion of investment and labor market covariates allow both studies to contribute unique perspectives to the literature.

2.2. The link between the macroeconomy and individual traits

More similar to the structure of this study are those which examine the impacts of macroeconomic events or conditions on social or psychological behaviors. Unlike the broad strokes with which studies of trust have been painted, analysis of the impact of macroeconomic events on behavior has a more narrow focus. Ehrmann and Tzamourani (2009) and Malmendier and Nagel (2011) document the negative relationship between past periods of inflation and current economic outlook. Mudd et al. (2010), Rioja et al. (2010), and Osili and Paulson (2009) examine the negative relationship between past experience of a banking crisis and persistent diminished levels of confidence in the banking system. Studies exist on the relationship between recessions and job prospects (Oreopoulos et al., 2006), political opinions (Kenworthy and Owens, 2010), and personal beliefs (Giuliano and Spilimbergo, 2009). Of particular note, Giuliano and Spilimbergo utilize regional U.S. survey data from the General Social Survey (whose questions often match those of the World Values Survey) to explore the effects of recessions on current beliefs, including interpersonal trust. They find no relationship between macroeconomic events and levels of trust, which is strongly contraindicated here in the context of Latin America. This may be due to the difference in economic history between the United States and the various different countries in Latin America, but may also be attributable to the focus of Giuliano and Spilimbergo on events experienced in the early teenage and adult years, rather than recent or concurrent recessions that are the focus of our current study. Ross and Escobar-Lemmon (2011) also utilize the World Values Survey to examine the relationship between trust and economic performance in Latin America specifically; they also generally find that economic conditions have no impact on trust, though this varies with horizontal and vertical trust channels and with the type of electoral system in the country.