



## Social capital and equilibrium selection in Stag Hunt games



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### ABSTRACT

Surveys of trusting attitudes are found to correlate with growth and development outcomes. The question of why trust attitudes correlate with economic growth remains open however. I argue that trust surveys capture facets of social capital not previously investigated, namely, coordination. Hence a complete investigation of the relationship between trust attitudes in growth must encompass their predictive power in a coordination game. This study shows that affirmative responses to surveys of trust attitudes correlate with and predict efficiency-supporting behavior in a Stag Hunt game.

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## 1. Introduction

Going back to at least Smith's *Wealth of Nations*, economists have studied why some societies are more prosperous than others. The "social capital" literature focuses on the role played by institutions, norms and beliefs that enable people to participate in mutually beneficial economic activities. Social capital can have many dimensions; but trust is thought to be crucial. Putnam (1993), contrasts local government effectiveness among the regions of Italy following power devolution in the 1970s. He finds that government effectiveness highly correlates with civic engagement<sup>1</sup> and generalized trust in others. Trust attitudes have standard measurement instruments found on surveys such as the General Social Survey and World Values Survey; and are found by cross-country studies, seminally Knack and Keefer (1997), to correlate with growth and other measures of institutional performance.

What mechanisms generate these reduced-form correlations? A literature has arisen in experimental economics seeking to tie trust attitudes to specific behavioral patterns that are candidates for generating macro-level outcomes. One model is the trust game studied by Berg, Dickhaut, and McCabe (1995). In that game, a sender decides how much money to transfer to

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<sup>1</sup> Putnam measures local government effectiveness as perceived citizen powerlessness, corruption, respect for the law and public safety. Putnam's civic engagement comprises referendum turnout, newspaper readership, number of sports and cultural associations in the community and the ability of political machines to enforce "preference voting".

a receiver. Money sent is multiplied; hence social surplus is maximized by sending the entirety of one's endowment. The receiver has the ability, but no obligation, to return some of the resulting surplus to the sender. For the sender to trust the receiver will return a monetary transfer is efficient, but not part of a Nash equilibrium. Glaeser, Laibson, Scheinkman, and Soutter (2000) however find that survey trust questions are not correlated with trusting behavior in the Berg et al. trust game. While trustworthy behavior (the receiver returning a sender's transfer) is correlated with survey trustworthiness questions, this is not the efficiency-generating action. A follow-on literature to Glaeser et al. confirms that behavior in the trust game is not robustly related to survey questions on trust. If the type of trust displayed in the trust game stands behind macro-level outcomes, it does not appear to be a channel through which trust attitude surveys are correlated with growth. We can respond to this finding in a number of ways. One is to focus on what trust game behavior is correlated with and build on those results. Another might be to dismiss the correlation between trust and prosperity as simply being generated by reverse causation: more prosperous societies instill trust in their citizens because people look backwards at a track record of success. Putnam himself argues against a causal interpretation of his data, emphasizing "path-dependent social equilibria" and saying that "Norms and networks of civic engagement contribute to economic prosperity and in turn are reinforced by that prosperity." Algan and Cahuc (2010) suggest that reverse causality is not solely responsible for observed data patterns, however. Their identification strategy argues for a causal interpretation of trust attitudes on growth – a result which demands further inquiry into the mechanisms generating it.

I argue that the ability to coordinate on efficient actions when they are risky is a form of social capital that can generate growth and prosperity. Social capital could be more than merely a question of finding Pareto-superior deviations from equilibrium play, however. Rather a society with substantial social capital may be successful in coordinating on Pareto-preferred equilibria. If trusting attitudes, revealed through standard survey measures, predict behavior in coordination problems this might explain why they are correlated with growth and other measures of institutional performance. This study establishes that trust surveys do predict behavior in a coordination game.

## 2. Social capital

The ability to exploit Pareto-improving opportunities in the face of uncertainty has profound relevance to economic development and entrepreneurship. Social capital is that which connects, directs, or otherwise enables economic activity. Dasgupta (2008) collects overlapping definitions:

'features of social organization, such as trust, norms, and networks that can improve the efficiency of society by facilitating coordinated actions' – Putnam, Leonardi and Nanetti (1993, p. 167);

'Social capital refers to connections among individuals – social networks and the norms of reciprocity and trustworthiness that arise from them.' – Putnam (2000, p. 19); and

'Social capital generally refers to trust, concern for one's associates, a willingness to live by the norms of one's community and to punish those who do not.' – Bowles and Gintis (2002, p. F419).

Social capital is most commonly measured with survey instruments on the General Social Survey or World Values survey. The standard 'trust question', found on both, is

'Generally speaking, would you say that most people can be trusted or that you can't be too careful in dealing with people?'

and will henceforth be referred to as *GSS\_trust*. Accompanying the standard trust question is a variant, also on both the GSS and WVS, the standard 'fair question'

'Do you think that most people would try to take advantage of you if they got the chance, or would they try to be fair?'

Trust attitudes are oft-used regressors in development and growth studies. Knack and Keefer (1997) correlate trust and civic norms as measured on the World Values Survey with measures of economic performance in a cross-section of 29 countries. These most prominently include growth, but also investment share of GDP, labor force growth, openness to trade, black market penetration, strength of property rights, currency depreciation, creditworthiness, and inequality. Knack and Keefer find that (WVS) trust has a positive correlation with these variables. La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1997) find that standard generalized trust measures track a very broad range of institutional and economic performance outcomes.<sup>2</sup> They argue that most organizations need to maintain trust among their members to function effectively: firms, nonprofits, and governments characterized by high trust and trustworthiness should perform better. Fukuyama (1995) makes a more discursive version of this argument. Higher trust enables organizations to grow larger since large organizations entail imperfect monitoring within the institution and greater reliance on norms of behavior to enforce cooperation among its members.

<sup>2</sup> These include efficiency of the judiciary, corruption, bureaucratic quality, tax compliance, civic participation, participation in professional associations, share of top 20 firms in GNP, adequacy/quality of infrastructure, infant mortality, high school completion, educational system adequacy, inflation, growth and GNP per capita.

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