Digital Receipt

This receipt acknowledges that Turnitin received your paper. Below you will find the receipt information regarding your submission.

The first page of your submissions is displayed below.

Submission author:	Lukas Purwoto
Assignment title:	Periksa similarity
Submission title:	Trust is Needed in Economic Development
File name:	Trust_is_Needed_in_Economic_Development.pdf
File size:	286.13K
Page count:	4
Word count:	2,857
Character count:	15,904
Submission date:	07-Mar-2023 01:31PM (UTC+0700)
Submission ID:	2031011882

Trust is needed in economic development

L. Purwoto & D. Utari
University of Sanata Dharma, Yogyakarta, Indonesia

ABSTRACT: A growing literature explains that societies could not function without a high level of trust and it also shows that trust is needed in the process of economic development. Some researchers argued that trusting others enables economic agents to operate more efficient and cooperative. This paper discussed previous results of the relationship between trust and growth. In line with others, the discussion supports the importance of any efforts in increasing and maintaining the high level of trust between every party that is involved in business transactions.

Keywords: trust, growth, economic development.

1 INTRODUCTION

The term trust has generally attracted the attention of academics, politicians, journalists, and various institutions. The government and state agencies emphasize the importance of trust between the government and the people. Politicians expect trust from their voters. Officials expect high trust in their institutions. Hopefully, the trust will be achieved in many sectors and by many parties.

Over the past two decades, trust has been one of the focuses of economic researchers concerned with economic development. Many claims suggest that societies will not be able to function without a high degree of trust and show that trust is necessary for economic growth and performance. Knack & Keefer (1997) suggested that the relationship between trust and growth is mainly found in poorer countries. Recently, Asongu & Gupta (2016) demonstrated that in countries with low quality of growth, decreased inequality and increased human development will enhance the positive relationship between trust and growth..

This article reviews previous studies, exploring both theoretical studies and empirical studies on the influence of trust in economic development. This article also performs statistical retest using the available data. The benefit of this article is to add a light discussion reviewing the literature in order to broaden our insights in a way that is simpler and easier to understand.

2 THEORITICAL ARGUMENT

Studies on the topic of social capital often use and show that trust is an important indicator of social capital. What is trust? Different authors may conceptualize trust in several ways, such as one-sided trust, reciprocal trust, and generalized trust. Under a one-sided trust, a trusting person or institution decides to act despite the uncertainty of the future and doubts about the reliability of the other party's promises. For example, according to Rose-Ackerman (2001), trust implies confidence, but not a certainty, that people or institutions will behave in the way they are expected. Farrell & Knight (2003) defined trust as a number of expectations held by the party that the other party will act in an appropriate way upon dealing with a specific issue. Similarly, Knack (2001) defined trust as a belief or perception by one party (the principal) that the other party (the agent) will not cheat on a particular transaction.

Laporta et al. (1997) suggested that prominent studies view trust or social capital as people's tendency within a society to work together in producing socially efficient results. The emphasized aspect here is the cooperation between people as a form of trust. Such condition describes a reciprocal trusting relationship, a condition where all participants are influenced by the attitude and behavior of the party standing on the other side of the transaction. While according to Durlauf & Fafchamps (2004), trust is understood as an optimistic belief or expectation related

ISBN 9786027385221

Trust is Needed in Economic Development

by Purwoto Lukas

Submission date: 07-Mar-2023 01:31PM (UTC+0700)
Submission ID: 2031011882
File name: Trust_is_Needed_in_Economic_Development.pdf (286.13K)
Word count: 2857
Character count: 15904

Trust is needed in economic development

L. Purwoto & D. Utari
University of Sanata Dharma, Yogyakarta, Indonesia

ABSTRACT: A growing literature explains that societies could not function without a high level of trust and it also shows that trust is needed in the process of economic development. Some researchers argued that trusting others enables economic agents to operate more efficient and cooperative. This paper discussed previous results of the relationship between trust and growth. In line with others, the discussion supports the importance of any efforts in increasing and maintaining the high level of trust between every party that is involved in business transactions.

Keywords: trust, growth, economic development.

1 INTRODUCTION

The term trust has generally attracted the attention of academics, politicians, journalists, and various institutions. The government and state agencies emphasize the importance of trust between the government and the people. Politicians expect trust from their voters. Officials expect high trust in their institutions. Hopefully, the trust will be achieved in many sectors and by many parties.

Over the past two decades, trust has been one of the focuses of economic researchers concerned with economic development. Many claims suggest that societies will not be able to function without a high degree of trust and show that trust is necessary for economic growth and performance. Knack & Keefer (1997) suggested that the relationship between trust and growth is mainly found in poorer countries. Recently, Asongu & Gupta (2016) demonstrated that in countries with low quality of growth, decreased inequality and increased human development will enhance the positive relationship between trust and growth..

This article reviews previous studies, exploring both theoretical studies and empirical studies on the influence of trust in economic development. This article also performs statistical retest using the available data. The benefit of this article is to add a light discussion reviewing the literature in order to broaden our insights in a way that is simpler and easier to understand.

2 THEORITICAL ARGUMENT

Studies on the topic of social capital often use and show that trust is an important indicator of social capital. What is trust? Different authors may conceptualize trust in several ways, such as one-sided trust, reciprocal trust, and generalized trust. Under a one-sided trust, a trusting person or institution decides to act despite the uncertainty of the future and doubts about the reliability of the other party's promises. For example, according to Rose-Ackerman (2001), trust implies confidence, but not a certainty, that people or institutions will behave in the way they are expected. Farrell & Knight (2003) defined trust as a number of expectations held by the party that the other party will act in an appropriate way upon dealing with a specific issue. Similarly, Knack (2001) defined trust as a belief or perception by one party (the principal) that the other party (the agent) will not cheat on a particular transaction.

Laporta et al. (1997) suggested that prominent studies view trust or social capital as people's tendency within a society to work together in producing socially efficient results. The emphasized aspect here is the cooperation between people as a form of trust. Such condition describes a reciprocal trusting relationship, a condition where all participants are influenced by the attitude and behavior of the party standing on the other side of the transaction. While according to Durlauf & Fafchamps (2004), trust is understood as an optimistic belief or expectation related to other agents' behavior. It is more like a generalized trust to other parties, which is a general attitude, instead of an evaluation towards relationships among particular persons.

Many claims state that societies will not be able to function without a high degree of trust and show that trust is necessary for the process of economic performance. How does trust affect economic development? There are two main reasons that not only apply to the country level but also to the company level. First, trust encourages cooperation and thus improves performance. According to Laporta et al. (1997), increased trust level between the people in a population should be associated with improved cooperation. Bureaucrats must cooperate with other bureaucrats they rarely meet and with private citizens they have never met in order to produce public commodities. Therefore, trust is needed to ensure cooperation. The performance of local government will be better in a high trust situation because trust allows a bureaucrat to work better with both other bureaucrats and private citizens, thus the government becomes more effective. So it is reasonable that trust may improve economic performance. Laporta et al. (1997) argued that trust is necessary to support cooperation in large organizations, such as the government. They also stated that corporations are big companies which will benefit from the trust among their employees.

The second reason is that high level of trust will lower the transaction costs. According to Knack & Keefer (1997), economic activities which require agents to rely on other agents' upcoming actions will be implemented at lower costs in an increasingly higher trust environment. Trust-sensitive transactions include the exchange of goods and services with an open account, employment contracts in which managers rely on employees to complete tasks which are difficult to monitor, as well as investment and savings decisions which rely on warranties made by the government or the bank that they will not expropriate the assets. They also argued that individuals in high trust societies may spend less to protect themselves from being exploited in economic transactions. A written contract is needed less and lawsuit is getting rarer. Individuals in a society with high level of trust will be less likely to divert their resources to protect themselves from criminal offenses against property rights such as bribery or private security services. In addition, low trust can reduce investment because when trust is low, contracts will not be able to be implemented without costly supervision and performance inspection by the contracting parties.

Akçomak & ter Weel (2006) also argued that low trust obstructs innovation. High social capital may eliminate problems and generate higher innovation output through the prevention of selfish behavior, changes in expectations, and decreased transaction costs. If entrepreneurs must devote more time to supervise the violations committed by partners, employees and suppliers, they will then have less time to create innovations in new products or processes. In this case, the costs of the supervision and the implementation of the contract are more likely to reduce investment returns and other economic transactions. Costly supervisions will also make investors reluctant to invest in corporate projects. Trust will also encourage the growth and accumulation of human capital. Bjørnskov (2004) argued that when interpersonal trust and honesty are low within a society, employers are very likely to face fraud in the form of work negligence, while in order to protect themselves; they tend to rely on information obtained during job applications rather than emphasizing formal formation such as education.

The theoretical model for reasons based on transaction costs was presented by Zak & Knack (2001). They presented a general equilibrium growth model in which agents do transactions and deal with moral hazard issues. The model describes the principal-agent structure, with investors as the principals and brokers as the agents in investment situations. Investors and brokers meet randomly and transact for a single period in which frauds performed by brokers are possible. They pointed out that fraud is possible (therefore reducing trust) when the social distance between agents is greater, formal institutions are weaker, social sanctions against fraud are ineffective, many greater investments exist, and investors' return is lower. More importantly, this model shows that the number of investments decreases when the social diversity is high and the formal and informal institutions are weaker, therefore causing negative impacts on the growth rate. So, trust, as well as institutional and social factors, will affect the growth. This model predicts that higher level of trust increases investment and growth. Finally, they suggested that this model may be generalized to other principal-agent relationships, like creditors and debtors, employers and employees, clients and consultants, and retailers and consumers.

3 EMPERICAL STUDIES

Indonesia is a country which recently attracted the attention of economic researchers on trust and social capital. Miguel et al. (2005) examined the effect of social capital on Indonesian factory laborers' growth from 1985 until 1995. They analyzed social capital and social interactions, including levels of trust, community activities, and informal cooperation. Olken (2006) examined the relationship between media acceptance and social capital in more than 600 villages in two provinces in Indonesia, Central Java, and East Java. The findings suggest that television and radio

ISBN 9786027385221

really diminish social capital, which is measured from the level of participation in social groups and social trust.

Empirical studies show that a high trust society produces high growth and economic performance. One of the first and most influential empirical studies in this field was performed by Knack & Keefer (1997). They investigated whether social capital – which are trust, networks, and norms of general cooperation – has economic results by researching internationally. From 29 countries used as samples, they found that trust and general cooperation norms have a strong influence on the average growth of annual per capita income and investment/GDP. Horizontal networks, which is measured by group memberships, are not related to trust and general norms and also economic performance. Laporta et al. (1997) examined the effect of trust on government performance, which is measured using various parameters related to efficiency (court efficiency, corruption, bureaucratic quality, and tax compliance), participation (general participation and participation in professional associations), sales of top 20 company/GDP, and social efficiency (infrastructure quality, infrastructure adequacy, infant mortality rate, high school completion, education system adequacy, inflation, and GDP growth). The results show that trust has a significant effect on performance. Using trust data from 41 countries, Zak & Knack (2001) confirmed the connection between trust and growth. Beugelsdijk et al. (2004) also provided similar international evidence. While at the regional level, Iyer et al. (2005) showed similar results in America and Ke & Zhang (2003) studied at the regional level in China.

Next, the authors are interested to recheck the study results of the previous researchers. The test uses a sample consisting of 63 countries, the same number used in the dataset used by Berggren et al. (2008), Asongu & Kodila-Tedika (2013), and Asongu & Gupta (2016). The dependent variable used is the annual growth of real GDP per capita (chained series), while the independent variable was the trust, which is obtained from the World Value Survey. This survey compiled a trust index by drawing samples from each participating country and asking respondents to answer general questions about trust.

Figure 1 plots the proportion of trust and economic growth into two dimensions. It is apparent that the observation points are spread with a positive associative tendency. Furthermore, the authors apply a regression model using the following formula based on the simplified version used in the previous studies:

$$Growth = \alpha + \beta Trust_i + \varepsilon_i \qquad (1)$$

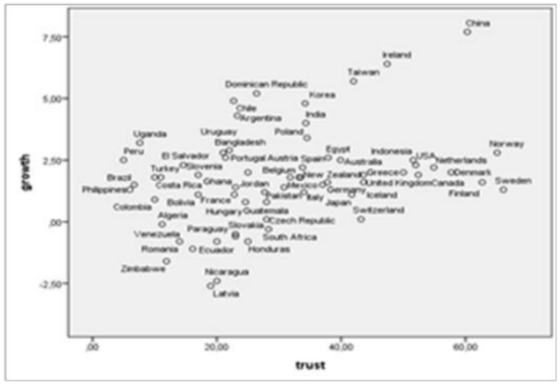

Figure 1. Scatter plot of trust and growth data of 63 countries.

Figure 2 shows the SPSS printout generated by the result of regression analysis on the relationship between trust and economic growth. The regression coefficient was found to be positive 0.042 and significant. The t-statistic is 2.854 and the p-value is 0.006. These results confirm the positive relationship between trust and economic growth as demonstrated by previous studies.

Coefficients[a]

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.
1	(Constant)	,467	,506		,922	,360
	trust	,042	,015	,343	2,854	,006

a. Dependent Variable: growth

Figure 2. SPSS printout from regression analysis for trust towards growth.

Recent empirical studies investigate the transmission channels in which trust affects economic growth. Studies show that innovation and human capital are the transmission channels. In the empirical investigation of 102 European regions within the period of 1990-2002, Akçomak & ter Weel (2006) found that higher innovations result in economic growth and social capital indirectly influences growth by encouraging innovation. Kaasa (2007) presented regional level evidence from Europe suggesting that social capital, which is measured using trust, relevant R&D expenditure, and the intensity of obtaining acquisition. In a sample consisting of 52 countries, Bjørnskov (2004) found that the influence of social capital, which is measured using trust, on the growth of human capital is significant. Likewise, Boulila et al. (2006) and Bjørnskov (2006) showed international result suggesting that trust influences economic growth through mechanisms such as education and investment.

The study on trust does not only examine its influence on economic development but also other social developments. Morris & Klesner (2010) examined the relationships between trust and corruption. Although the causality is still debatable. Lederman et al. (2002) examined the impact of social capital, which is measured using trust and participation in voluntary organizations, on criminality.

Thus, all those findings provide important implications for public policymakers and other institutions, promoting the importance of increasing trust. Knack & Zak (2002) suggested that we can increase trust by strengthening law and reducing injustice. In line with this suggestion, Rothstein & Uslaner (2005) pointed out that trust is caused by two types of justice, namely economic equity, and opportunity equity.

4 RESULT AND DISCUSSION

This article reviews the growing literature on trust. Various earlier studies have shown that trust is a decisive factor which is not trivial in explaining economic and corporate development. Trust lowers transaction costs and encourages cooperation so as to increase human capital and create innovation that ultimately produces higher growth and performance. A high trust company will gain competitive advantages that are useful in resolving various problems and causing lower expenditures which are beneficial in contract implementations with various parties.

REFERENCES

Akçomak, I.S., & ter Weel, B. 2006. Social capital, innovation and growth: evidence from Europe. *UNU-MERIT Working Paper*.

Asongu, S.A. & Kodila-Tedika, O. 2013. Trust and prosperity: a conditional relationship, *MPRA Paper No. 46865*.

Asongu, S.A. & Gupta, R. 2016. Trust and quality of growth: a note, *Economics Bulletin*, 36(3): 1854-1867.

Berggren, N., Elinder, M., & Jordahl, H. 2008. Trust and growth: a shaky relationship, *Empirical Economics* 35(2): 251-274.

Beugelsdijk, S., de Groot, H., & van Schaik, A. 2004. Trust and economic growth: a robustness analysis. *Oxford Economic Papers* 56: 118-134.

Bjørnskov, C. 2004. Social capital and the growth of human capital. *Working Paper, Aarhus School of Business*.

Bjørnskov, C. 2006. How does social trust affect economic growth? *Working Paper, Aarhus School of Business*.

Boulila, G., Bousrih L., & Trabelsi, M. 2006. Social capital and economic growth: empirical investigation on the transmission channels. *Working Paper, Ecole Supérieure des Sciences Economiques et Commerciales*.

Durlauf, S.N & Fafchamps, M. 2004. *Social Capital. The Centre for The Study of African Economies*. The Berkeley Economic Press.

Farrell, H. & Knight, J. 2003. Trust, institutions, and institutional change: industrial districts and the social capital hypothesis, *Politics & Society* 31: 537-566.

Iyer, S., Kitson, M., & Toh, B. 2005. Social capital, economic growth and regional development, *Regional Studies* 39: 1015-1040.

Kaasa, A. 2007. Effects of different dimensions of social capital on innovation: evidence from Europe at the Regional Level. *Working Paper*.

Ke, R. & Zhang, W. 2003. Trust in China: a cross-regional analysis. *William Davidson Institute Working Paper*.

Knack, S. & Zak, P.J. 2002. Building trust: public policy, interpersonal trust, and economic development, *Supreme Court Economic Review* 10: 91-107.

Knack, S. 2001. Trust, associational life and economic performance. In John Helliwell (ed.), *The Contribution of Human and Social Capital to Sustained Economic Growth and Well-Being: International Symposium Report*. Quebec: Human Resources Development Canada.

Knack, S., & Keefer P.P. 1997. Does social capital have an economic payoff? a cross-country investigation, *Quarterly Journal of Economics* 112: 1251-1288.

LaPorta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. 1997. Trust in large organizations, *American Economic Review Papers and Proceedings* 87: 333-338.

Lederman, D., Loayza, N., & Menendez, A.M. 2002. Violent crime: does social capital matter? *Economic Development and Cultural Change*: 509-539.

Miguel, E., Gertler, P. & Levine, D.L. 2005. Does social capital promote industrialization? evidence from a rapid industrializer. *Review of Economics and Statistics* 87: 754-762.

Morris, S.D. & Klesner, J.L. 2010. Corruption and trust: theoretical considerations and evidence from Mexico, *Comparative Political Studies* 43(10): 1258-1285.

Olken, B.A., 2006. Do television and radio destroy social capital? evidence from Indonesia villages. *NBER Working Paper*.

Rose-Ackerman, S. 2001. Trust, honesty, and corruption: reflection on the state-building process, *Archive of European Sociology* XLII: 526-570.

Rothstein, B. & Uslaner, E.M. 2005. All for all: equality, corruption, and social trust. *World Politics* 58: 41-72.

Zak, P.J. & Knack, S. 2001. Trust and growth. *Economic Journal* 111: 295-321.

ISBN 9786027385221

Trust is Needed in Economic Development

ORIGINALITY REPORT

16%	7%	12%	4%
SIMILARITY INDEX	INTERNET SOURCES	PUBLICATIONS	STUDENT PAPERS

PRIMARY SOURCES

1	ediss.uni-goettingen.de Internet Source	2%
2	Paul J. Zak. "Trust and Growth", The Economic Journal, 04/2001 Publication	2%
3	Ghazi Boulila, Lobna Bousrih, Mohamed Trabelsi. "Social capital and economic growth: empirical investigations on the transmission channels", International Economic Journal, 2008 Publication	1%
4	Submitted to University of Cambridge Student Paper	1%
5	Steven J. Bosworth. "Social capital and equilibrium selection in Stag Hunt games", Journal of Economic Psychology, 2013 Publication	1%
6	openjournals.uwaterloo.ca Internet Source	1%
7	Submitted to Sunway College Student Paper	

1%

8	mafiadoc.com Internet Source	1%
9	Submitted to Queen's University of Belfast Student Paper	1%
10	Stephen Knack. "Does Social Capital Have An Economic Payoff? A Cross-Country Investigation*", Quarterly Journal of Economics, 11/1997 Publication	1%
11	Submitted to UC, San Diego Student Paper	1%
12	Jesús Peiró-Palomino. "Social Capital and Economic Growth in Europe: Nonlinear Trends and Heterogeneous Regional Effects", Oxford Bulletin of Economics and Statistics, 2016 Publication	1%
13	Submitted to London School of Economics and Political Science Student Paper	1%
14	Paula Puskarova. "Trust or bust: Growth effects of knowledge, human and social capital revisited", Economic Systems, 2022 Publication	1%

15	Cheng Zhang, Kung-Cheng Ho, Cheng Yan, Yujing Gong. "Societal trust and firm-level trust: Substitute or complement? An international evidence", International Review of Financial Analysis, 2023 Publication	<1 %
16	pure.au.dk Internet Source	<1 %
17	www.nek.uu.se Internet Source	<1 %
18	Antonio C. David, Carmen A. Li. "Exploring the links between HIV/AIDS, social capital and development", Journal of International Development, 2010 Publication	<1 %
19	Devesh Roy, Abdul Munasib, Xing Chen. "Social trust and international trade: the interplay between social trust and formal finance", Review of World Economics, 2014 Publication	<1 %
20	Isaac K. Ofori, Camara K. Obeng, Simplice A. Asongu. "What Really Drives Economic Growth in Sub-Saharan Africa? Evidence from the Lasso Regularization and Inferential Techniques", Journal of the Knowledge Economy, 2022 Publication	<1 %

21	Kodila-Tedika, Oasis, and Julius Agbor. "Does Trust Matter for Entrepreneurship: Evidence from a Cross-Section of Countries", Economies, 2016. Publication	<1 %
22	ageconsearch.umn.edu Internet Source	<1 %
23	core.ac.uk Internet Source	<1 %
24	www.ppge.ufrgs.br Internet Source	<1 %
25	Mahyudin Ahmad, Stephen G. Hall. "Trust-based social capital, economic growth and property rights: explaining the relationship", International Journal of Social Economics, 2017 Publication	<1 %
26	"What Have We Learned About Generalized Trust, If Anything?", Annual Review of Political Science, 06/2008 Publication	<1 %

Exclude quotes On
Exclude bibliography On
Exclude matches < 5 words