

Unpacking Social Capital in Economic Development: How Social Relations Matter

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Abstract Social capital is a contested concept, embraced by the mainstream as “the missing link” in economic analysis. This article suggests a way to turn it into a more meaningful understanding of how social relations matter in the economy. It will do so by unpacking the concept into various elements, distinguishing what social relations are from what they do, and by recognizing power in social relationships. We will illustrate our alternative approach with two case studies on the Small and Medium scale Enterprises (SME) footwear sector in Ethiopia and Vietnam. We conclude with suggestions on how this more contextual approach to the understanding of the economic influences of social relations may contribute to social economics.

Keywords: social capital, trust, SME, footwear, Ethiopia, Vietnam

INTRODUCTION

The most general definition of social capital is that “relations matter”. If this were the only insight from the burgeoning literature on the topic, it does not bring much news to social economists. To the contrary, the insight that social relations matter to the economy has been the very foundation of social economics for more than half a century—long before the discovery of the social capital concept by economists. Indeed, what has been portrayed as “the missing link” by mainstream economists is common knowledge among social economists. The social capital literature, hence, seems another example of the economist searching for his lost keys under a lamp post while he lost them in a dark alley.

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True as this may be, such a self-congratulating view about social capital is likely to ignore recent developments analysing in what specific ways social relations appear to affect economic decisions and processes, and how social economic processes influence the accumulation, distribution, and effectiveness of social capital. Rather than regarding social capital as just another variant of capital and reducing it to a variable in a regression analysis, a small but innovative body of research has developed that is actually unpacking the black box of the connections between social relations and economic outcomes. Such studies have particularly emerged in the area of development economics. This is probably due, at least in part, to the fact that the World Bank has taken on board the concept a decade ago, which was quickly followed by an ambitious research initiative by the Bank.¹ Another reason why it is particularly in development studies that social capital has received relatively much attention is given by Durlauf and Fafchamps (2004), who state that it has been found useful to address the complex, society-wide problems of poverty in developing countries.

In this article, we will also engage with social capital in the context of development, drawing on two case studies on the footwear sector in Vietnam and Ethiopia (Knorringa and van Staveren 2006).² Our objective is to point out not *that* social relations matter, but *how* they matter to the economy: how can social capital be understood from a social economic perspective? And, subsequently, what does this insight contribute to the vast body of knowledge in the area of social economics? In other words, does the social capital literature, and in particular research arising in the area of development studies, contain value added for social economics, or is it merely old wine in new bottles?

In order to address this question, the article is structured as follows. The next section will start with a brief, necessarily partial, overview of the literature on social capital in economics, focusing on development. This overview will be followed by a critique and a discussion of the problems, which includes both theoretical and empirical concerns. The third section will

1 See World Bank (1998) and the following website: <http://lnweb18.worldbank.org/ESSD/sdvext.nsf/09ByDocName/SocialCapitalInitiativeWorkingPaperSeries>

2 These case studies were carried out for the United Nations Industrial Development Organization (UNIDO) in a research project on the operationalization of social capital for industrialization in marginalized developing countries. In this article we draw on some of the work we did for this research project. We would like to express our gratitude to the colleagues who have worked with us on that project: Tseguereda Abraham, Tegegne Gebreegzabher, Albert H. J. Helmsing, Adam McCarty, Lee Pegler Bethel Terefe, Luong Thanh and Thanh Dam Truong. A special thanks also to Jorg Meyer-Stamer, Mike Morris and Hubert Schmitz, and, finally, we would like to thank our counterparts at UNIDO for their support and helpful suggestions during the project.

lay out an alternative, social economic approach to social capital. The fourth section will present the two case studies, applying the social economic approach, while the last section will provide a conclusion.

ECONOMIC LITERATURE ON SOCIAL CAPITAL

Theoretical Integration

In most of the literature social capital has been integrated into mainstream economic models. Since mainstream economics adheres to methodological individualism, the literature pictures social capital as a property of individuals. As a consequence, social capital effects on communities, organizations and countries are deduced from rational choices made by individuals. In the empirical literature, social capital has been captured by measuring trust, group membership, and civic norms.³ Generally speaking, there are three different ways in which social capital is integrated in the economic mainstream. First, social capital is pictured as a preference in utility functions (Becker 1996; Glaeser *et al.* 2000). Second, it is perceived as an individual resource, owned by individuals or firms (Bourdieu and Wacquant 1992; Van der Gaag and Snijders 2004; Paldam and Tinggaard Svendsen 2004). Third, social capital is regarded as an instrument to reduce risks. Some of this literature is framed in a bargaining approach (Hargreaves Heap 1999; Moore 1999; Dasgupta 1999; Paldam 2000; Torsvik 2004), while others have employed a transaction costs approach (Grabowski 1998; Szreter 2000; Paldam and Tinggaard Svendsen 2004).

These three ways in which the mainstream has integrated social capital has met with strong critiques from heterodox traditions. Most of the critiques start with a critical discussion of the name of the concept, and the metaphorical implications of the word “capital”. It is precisely the view of social capital as an independent resource of individuals, firms and organizations, which has raised much critique on the World Bank approach to social capital (Harriss and de Renzio 1997; Fox 1997; Fine 1999, 2001; Fox and Gershman 2000; Harriss 2001). It assumes that social capital may substitute for public goods and government regulation simply by stimulating individuals to engage in clubs, associations and other forms of engaging with each other. But such a view, the critics argue, ignores persistent power asymmetries that

3 Trust is almost exclusively measured in surveys with the World Values Studies (WVS) trust question: “Generally speaking, would you say that most people can be trusted, or that you can’t be too careful in your dealings with people?” Information about the WVS can be found at the following website: <http://www.worldvaluessurvey.com/>

are part of society, resulting in exclusion, inequality and control in and between groups of people (Field 2003).

A second critique addresses the instrumental view of social relations in the mainstream social capital literature. Such a view denies that social relations are ends in themselves, and do not necessarily (need to) generate economic benefits. In particular, the utilitarian conceptualization of social relations instrumentalizes human relations which, in the end may not lead to positive utility effects (van Staveren 2000). Trust has been defined, for example, as rational expectations of the behaviour of others (Dasgupta 1999: 330). One of the criticisms of such understanding of trust comes, surprisingly, from Oliver Williamson (1993) who argues that this instrumental view of trust confuses credibility, which derives from calculable risk, with the ethical value of trust. He therefore states that “calculativeness will devalue the relation” (Williamson 1993: 484) since it “may well be destructive of atmosphere and lead to a net loss of satisfaction between the parties” (p. 481).

A third line of critique on the mainstream use of social capital concerns the empirical literature. One of the most central flaws that has been recognized in the empirical literature is a circular explanation of social capital: a group’s success is attributed to its social capital, but social capital is measured by group success (Durlauf 2002). Often, the measurement of group membership fails to distinguish between types, purposes and structures of groups as well as power relations within and between groups (Hoerber Rudolph 2000). Moreover, as Diani (2004) has suggested, associations may reflect distrust in government and political institutions—associations may be a response to this distrust rather than a reflection of general trust, beyond the boundaries of associations. Another empirical problem is that measuring social capital by aggregating individual group membership ignores the fallacy of aggregation in a social context (Glaeser *et al.* 2000; Durlauf and Fafchamps 2004). Moreover, critical empirical research indicates that some variables may be contradictory, such as trust and group membership, or strongly relate to contextual variables, such as trust and inequality, which seem to be negatively correlated, suggesting that inequality and hierarchy should also be taken into account when measuring social capital. When measuring social capital not as group membership but as trust, similar criticisms apply (see, for an in-depth discussion of trust, Nooteboom 2002). Edwards and Foley (1997) as well as Baron *et al.* (2000) have noted that trust is often affected by power relations, which result in inequalities having a negative impact on trust. The critiques on the empirics of social capital suggest that a more realistic approach to social capital research would need to unpack the concept, both theoretically and empirically (Durlauf and Fafchamps 2004).

In conclusion, the critics of the mainstream approach to social capital see the way in which it has been absorbed in the neo-classical paradigm as still not really acknowledging the social in the economy (see, for example, Elster 1995; Fine 1999 and 2001). Ben Fine (2001) and John Harriss (2001) do not see much value added in the concept used this way, since they find it molded into the straightjacket of methodological individualism, ignoring issues of power, conflict and class. Fine therefore prefers to study social, political, and cultural dimensions of economic processes from the perspective of political economy instead. In this paper we sympathize with Fine and other critics, but tolerate the label for the sake of carrying the discussions between various schools of economic thought on how social relations matter a bit further.

TOWARDS A SOCIAL ECONOMIC THEORY OF SOCIAL RELATIONS

In this section we begin to sketch a social economic theory of social relations, aiming to overcome the instrumental view towards social relations and the circular reasoning in the mainstream social capital literature. In our view, two main pillars of such a social economics approach are, first, a more nuanced understanding of both the intended and unintended effects of social relations on economic outcomes, including the potentially perverse effects of power asymmetries. A second pillar involves a more careful empirical operationalization that overcomes circular reasoning through clearly distinguishing between what social relations are, and what they do.

To begin with, critical studies of social capital have acknowledged that social relations are not necessarily positive, and neither are their economic impacts. Social structures inevitably incorporate power asymmetries that lead to processes of inclusion and exclusion, on the basis of certain discriminating criteria, to relationships of authority and control, as well as to inequalities between people that could range from implicit differential treatment to sheer oppression of one group by another. As a consequence, social capital can have a perverse character, involving societal costs, such as undemocratic tendencies, and economic costs, such as rent seeking and discrimination (Baron *et al.* 2000; Fine 2001; Molyneux 2002; Bowles and Gintis 2002; Taylor and Leonard 2002; Field 2003; Dolfisma and Dannreuther 2003).

The influence of power asymmetries on social capital is complex. Fox (1974: 95) already recognized the inherent contradictions between power and social capital by pointing out that in situations of extreme inequality, trust transforms into accepting one's lack of choice rather than being an

expression of a society's social capital: "We've got to trust them" means in fact: "we don't trust them but feel constrained to submit to their discretion". This simply describes, of course, a power relationship. The literature on social capital and power suggests that the relationship is often negative, that is, social capital appears to be less effective in situations of inequality, control, and exclusion (Edwards and Foley 1997; Baron *et al.* 2000; Fine 2001; Harriss 2001; Molyneux 2002; Taylor and Leonard 2002; Dolfisma and Dannreuther 2003; Field 2003). But the relationship between social capital and power is even more complex. At the same time, beneficiary effects of social relations may be brought about precisely through power asymmetries, not by trust. It is important not "to ignore the fact that power can be hidden behind a façade of "trust" and a rhetoric of "collaboration" and can be used to promote vested interests through the manipulation and capitulation of weaker parties" (Hardy *et al.* 1998: 65).

In order to bring some clarity on the possible relationships between social capital and inequality, Field (2003: 74) has listed four ways in which the two may be related:

- access to different types of networks is unequally distributed;
- social capital in networks can be used to disadvantage others;
- social capital in groups can benefit members but reproduce inequality or generate unintended consequences for others;
- social capital can have a leveling-down effect on people's aspirations, providing disincentives for individuals in a group to save and invest.

Next to power, also other social relations make part of the creation, distribution and effectiveness of social capital. These are, among others, solidarity, social cohesion, patronage, domination, prestige, reputation, trust, sociability, and organization (see also the critique of Fine 2001).

As a consequence of this diversity of social relations underlying social capital, we cannot hope for a very sharp definition of social capital. Nevertheless, our working definition is that social capital can be seen as "the set of social relations that enable actors to gain, maintain or expand access to economic resources that may lead to the reinforcement of the productivity of these economic resources". However, more important than detailed debates on the exact and appropriate definition of social capital, we side with Edwards and Foley (1997: 677), who hold that social capital points "analytical attention to the embeddedness of cultural factors—such as identities and aspirations—in the meso level social structures such as neighborhood, church, family, school and voluntary associations. These are

relational contexts in which understanding of how the world works, orientations toward it, and how to engage it are embedded, produced and reproduced in a continuous process of construction, negotiation and appropriation.” Here, the critical social capital literature shows a remarkable similarity with social economics. The critics of the social capital mainstream as well as heterodox economists who interpret, analyse, and reconstruct the concept and use it carefully in empirical studies, do appear to rely on insights of social economics—consciously and sometimes, perhaps, not so aware of this tradition of economic thought. In their critical volume on social capital, Baron *et al.* (2000: 35) have distinguished five characteristics of an alternative social capital approach. In this approach, they conclude, social capital shifts the focus of analysis from the behaviour of individual agents to patterns of relations between agents, social units and institutions, linking micro, meso, and macro levels of analysis, and reinserts morality into economic analysis. Since social economics is concerned with values, social interaction, non-reductionism, and inter-disciplinarity, it does indeed seem to offer a suitable home for an alternative analysis of how social relations matter in the economy. This can be seen, for example, from the characterization of social economics by Mark Lutz:

Social economics is an economics centered around and directed by certain basic value premises or ethical postulates. It critically examines the mutual interaction between economic valuations (including observed individual psychological dispositions), economic activity (including work, consumption, technological innovation), and economic institutions (including uncoordinated, free market mechanisms, and financial institutions; ownership of property and rules of appropriation; social relations of production and the wage system) in the light of those basic value premises. (...) In the process the market is rejected as a final arbiter of social values and instead priority is given to a non-reductionistic, holistic ethos intrinsically related to a conception of society as an organic whole. (Lutz 1990: 416–17)

Other social economists have also emphasized the relationship and interaction between the individual and the social, including moral dimensions. For example, Edward O’Boyle (2005) has characterized social economics as being concerned with meeting human material needs, which partly occurs through processes of belonging. In his systematic characterization of social economics, Hunt (2005) has distinguished three criteria: first, a recognition of the interaction between the individual and social relations; second, a recognition of the normativity of addressing human needs; and, third, a concern with institutions and their capacity to address human needs.

Combining the directions for an alternative to social capital theory with the heart of the social economic approach, we now continue to present a preliminary sketch of a social economic theory of social relations. The starting point for such a theory is an understanding of social capital at the inter-personal level, as arising out of, largely, intentional social relationships, embedded in a community's—moral—values and beliefs, as expressed in institutions. A distinguishing feature of social capital in a social economic approach is that it is not instrumental, or at least, not in the first place. If friendships, for example, would come about in this way, it is very unlikely that they would last in a similar way as they do in the real social world, according to Elster (1983). The basis of social capital, hence, is social cohesion in groups and communities, social relations in societies, and network relationships between individuals and groups, which express underlying shared—and contested—values, as well as power, and which may have positive as well as negative social and economic effects.

Bonding and Bridging Social Capital

Before we will go into the intended and unintended economic effects of social relations, we first need to introduce an important typology of social capital. The more recent social capital literature distinguishes between two levels of social capital, referred to as bonding and bridging social capital (Woolcock 1998, 2001; Putnam 2000).⁴ What we would like to emphasize about this distinction—and what the mainstream literature does not recognize—is that it reflects a power asymmetry, namely the one of inclusion/exclusion.

Bonding social capital emerges from strong social ties, which are based on a social identity, for example family and kinship, gender, ethnicity, religion or organizational culture. As a consequence of the social cohesion in a group, bonding social capital generates a particular type of trust that is ascribed to the members of the group: “I trust you because you are a member of my clan.” Through norms that groups establish for their functioning, they have the opportunity to control trust to a certain extent, for example by punishing those who take advantage of the trust ascribed to them. Ascribed groups are relatively closed and exclude others who do not happen to share the same distinguishing characteristic. Hence, bonding social capital may create

4 Woolcock's differentiation is slightly different because he adds a third type, namely linking social capital, which comes close to what in the heterodox literature has been understood as bridging social capital. His notion of bridging social capital is an intermediate step between bonding and linking social capital (see Woolcock 2001: 13–14).

segmented markets with entry barriers for non-group members (see, for example, Bowles and Gintis 2002). On the other hand, such groups tend to generate high levels of trust, cooperation, and organization, facilitating collective action and learning. As Massimo Repetti (2002) has remarked for various African countries, production is often based on close (family) ties, including patterns of subordination and paternalism, as well as practices of sharing resources and redistribution of profits.

Bridging social capital emerges from weak social ties across society in which individual and organizational behaviour is embedded (Granovetter 1985), but which is nevertheless held together through diverse group memberships and the sharing of some common values.⁵ Weak ties exist among members of social groups that are heterogeneous, having different social identifications. Weak ties can occur horizontally, creating networks between loosely connected individuals, organizations and groups, as well as vertically, in hierarchical relations. These are much more open relations, compared with those of bonding social capital, relying on earned trust among loosely connected people rather than on ascribed trust among a homogenous, strongly related group. Bridging social capital generates what is labelled generalized trust, which is based on the belief that everyone shares a minimum set of common values and therefore has a minimum level of trustworthiness to act upon these values. Generalized trust is not blind trust, a belief in the unquestioned goodness of everyone in which trustworthiness is considered to be beyond doubt, but it often includes checks and balances of the others' trustworthiness, in particular through the assessment of a person's reputation over time and rewarding trustful behaviour through reciprocity of trust (see also Humphrey and Schmitz 1998, on the distinction between ascribed and generalized trust). Bridging social capital enables the emergence of economic transactions between strangers and helps to reduce the inevitable transaction costs arising from incomplete contracts and uncertainty.

The two categories of social capital are not mutually exclusive. An economy needs both types of social capital. It requires a minimum level of bonding social capital for bridging social capital to emerge. Bonding social capital generates externalities for individual agents' behaviour from group practices, creating and reproducing certain social capabilities, for example the adherence to social norms, which may include mutual help, trustworthiness,

5 It is important to note that the word "weak" should not be interpreted negatively here, since, paradoxically, the weakness in the ties is the strength of bridging social capital: social relationships are voluntary, continuously leaving open the option of breaking up or changing one relation for another, without strong social sanctions.

sociability, solidarity, loyalty and responsibility, as well as knowledge sharing. Bridging social capital builds on these social capabilities—it will not just arise by itself in a society without any experience of close bonds between people in families, friendships, associations and organizations. The relationship between the two, however, is not straightforward: the two levels of social capital seem to be partly trade-offs and partly supporting each other. Weak social ties tend to have the highest economic benefits, as generalized trust connects a broader, more diverse group of people and their human, financial and other resources.⁶ Hence, bridging social capital is likely to be more beneficial than bonding social capital through a wider spread of positive externalities of social norms, although without bonding social capital there is no fertile ground for bridging social capital to develop.

Too much bonding social capital can cause constraints, if it is not complemented by bridging social capital. If people deal only with members of their own group, they run the risk of getting “locked-in” into a limited economic realm that is not very innovative or efficient in terms of resource allocation. Too much bonding social capital can exclude others from social capital generation—others who have either no groups to share social capital, or who are members of less influential groups with limited access to resources. Moreover, bonding social capital could lead to the formation of cartels between firms; and could allow some groups of entrepreneurs to enjoy more advantages than others, for example when male entrepreneurs are allowed easier access to and control over credit than female entrepreneurs.⁷ Furthermore, bonding social capital may enable rent-seeking as it may connect entrepreneurs to government officials belonging to the same social group. In other words, power asymmetries in social capital are often beneficial for those who are in high positions, but can create a net welfare loss for society. Hence, bonding social capital sometimes appears to be perverse social capital: it benefits a privileged minority but creates costs for the excluded. Finally, too much bonding social capital can reduce the generation of bridging social capital when the norms of conformation to the group do not allow for the development of weak ties with outsiders. As Douglas Caulkins (2004), for example, has found in his research in Norway on bonding and bridging ties, the bonding ties of group membership do not

6 Durlauf and Fafchamps (2004) give a partially different reason for the greater efficiency gains from general trust, compared to ascribed trust. They argue that generalized trust is established faster and more cheaply. This is questioned, however, in literature emphasizing how difficult it is to move from ascribed to generalized trust.

7 See for example research on social capital and gender inequality for female entrepreneurs in credit through group-lending: Linda Mayoux (2001), Katherine Rankin (2002), and Maxine Molyneux (2002). See also a discussion of gender inequality in relation to social capital by van Staveren (2003).

necessarily enable the generation of bridging ties across groups. In other words, he found no support for the hypothesis in Putnam's seminal work, that "the greater the organizational density, the greater the social capital and generalized trust" (Caulkins 2004: 178).

So, a society may economically benefit from a transformation of bonding social capital into bridging social capital by moving away from smaller group identities toward shared social values, allowing for more interactions between a wider variety of social identities and group memberships.

Social Relationships: What They Are and What They Do

To arrive at a more robust operationalization of how social relations matter, which avoids circular reasoning, it is important to clearly distinguish between what social relations are, and what they do.⁸ Above we have already presented our working definition of what social capital is, which characterizes the economic influences of social relations as enabling actors to gain, maintain or expand access to economic resources which may lead to a reinforcement of the productivity of these economic resources.

In terms of "what they do", social relations may lead to a variety of potential economic benefits to actors that are engaged in such relevant social relations (Dasgupta and Serageldin 1999; Baron *et al.* 2000; Grootaert and van Bastelaer 2002; Collier 2002; Flap 2004). Some of these potential benefits are mentioned more often than others and seem to draw on a wider common understanding. We have grouped these into three types of economic impacts: (1) reducing transaction costs; (2) enabling and reinforcing of collective action; and (3) generating learning spin-offs. As a result of our argument above on the importance of power asymmetries, one needs to always carefully scrutinize where and when these benefits (may) turn into gains for a small group, at the cost of others and sometimes even at the cost of inefficiencies for the economy as a whole.

1. Reducing transaction costs

Here, the underlying mechanism of social relations is the moral value of trust. Trust fills in gaps in incomplete contracts and in monitoring (in particular in uncertain environments), which saves time and money. Trustworthy behaviour, in turn, helps to build a reputation, which is

⁸ For, example it has been suggested that trust may be more appropriately regarded as an *outcome* of social capital rather than a *determinant* of it (Field 2003: 65 and 125).

likely to generate even more trust, further reducing transaction costs. Trustworthiness hence helps to reduce the likelihood of free-riding in public goods as well as rent seeking and moral hazard. Trust can therefore be understood as “the confidence that parties will work for mutual gain and refrain from opportunistic behavior” (Cooke and Morgan 2000: 30). It reduces transaction costs because it enables parties to economize on time and effort, which generates the efficiency of being able to rely on the word of one’s partner. An interesting empirical study by Fafchamps and Minten (1999) on the benefits of social capital for agricultural traders reveals, for example, a reduction in transaction costs among traders through trust in interaction, access to credit, information on prices and economies of scale in quality control. But the economic effects of reducing transaction costs may be negative for the economy as a whole. For example, the elite may succeed in tax evasion and evading democratic procedures by bribing government officials. The bribe creates a social relationship of power that has benefits for both parties but at a cost to the economy at large.

2. Enabling and reinforcing collective action

In this case, the underlying mechanism of social relations is solidarity and cooperation. Cooperation between individuals and organizations creates economies of scale, and helps to provide and manage semi-public goods (outside the state) or enforces the supply of public goods by the state. In a context of uncertainty, trust reduces the risks of cooperation and discloses possibilities for action which would have been unattractive otherwise (Cooke and Morgan 2000: 30–31). Such trust-confirming cooperation can also enhance bargaining power in the market, leading to increased access to, or better negotiation terms in markets. But collective action can also have negative economic impacts. For example, processes of exclusion by a group could lead to market segmentation, setting up entry barriers for certain groups in, for example, the credit or labour market. Alternatively, collective action could result in market power in the case of cartels. Again, these benefit a small group at the cost of others, such as the unemployed in the case of labour markets.

3. Creating learning spill-overs

Here, the underlying mechanism of social relations is social cohesion and sociability. By working together, workers learn from each other on the job. This process is stimulated in a setting of teamwork, where new team members learn on the job under the guidance of workers who are more experienced. A dynamic workforce, in particular when it is a specialized workforce possessing special skills, helps to transmit human capital

through learning from one company to another—a feature of human capital expansion that is also drawn upon in endogenous growth theories. Another form of learning spill-overs is through collective learning by jointly acquiring or quickly transmitting new technology, for example, through business networks (Porter 2000). In both ways—by increasing the average level of human capital and transmitting new technology—social cohesion and sociability enhance total factor productivity. The transmission of information is also helped by trust, which helps to overcome transaction costs in the transmission process, as participants in high-trust relationships tend to have a greater capacity for learning because they are party to thicker and richer information flows (Cooke and Morgan 2000: 31). But learning spill-overs may also be affected by power asymmetries. It is quite likely that spill-overs will occur much less, or not at all, in a work environment with high inequality. In such an environment, the opportunities and social incentives to learn from other entrepreneurs or workers are limited. Besides, collective learning in a sector will be constrained by high inequality, as not all firms will be allowed access to the collective learning process.

The above section has sketched the contours of a social economic theory of how social relations matter in the economy, but with many question marks and blank spots. It is no more than a beginning, which, hopefully, could develop into a more coherent understanding of the role of social relations in the economy than the mainstream theory of social capital that faces such serious problems, as we have discussed above. As a way to get more grips on the picture sketched in this section, the next section will present a summary of two case studies, applying some of the insights that were presented here, by paying careful attention to the measurement of influences of social relations, the meaning of the underlying social relations, and the types of economic impacts.

TWO CASES OF THE FOOTWEAR INDUSTRY

The data on the two case studies discussed in this section have been collected as part of a UNIDO research project on operationalizing social capital for industrial development. Given UNIDO's strategic priorities, and considering our previous experience and existing networks, we were invited to undertake a literature review and two exploratory case studies on small and medium scale enterprises (SMEs) in the footwear industry in two marginalized, low-income countries: Ethiopia and Vietnam (Knorringa and van Staveren 2006).

Social Relations in SME Industrial Development

For the operationalization of the approach sketched above for our case studies of SMEs in industrial development, we have made use of the literature on inter-firm relationships, clusters, value chains, business associations and business systems (see, for example, Coleman and Jacek 1989; Amin and Thrift 1994; Evans 1996; Hyden 1997; Humphrey and Schmitz 1998; Meyer-Stamer 1998; Maskell and Malmberg 1999; Gereffi 1999; Cooke and Wills 1999; Knorringa 1999; Schmitz 1999; Moore 1999; Schmitz and Knorringa 2000; Asheim and Isaksen 2000; Mumvuma 2000; Humphrey and Schmitz 2000; Helmsing 2001; Jacobsen and Torp 2001; Taylor and Leonard 2002). There is no space in this article to review this literature, so we will summarize here the major connections that we found with the subject of this article:

- Clusters are more likely to initially rely on bonding ties; successful clusters are often characterized by high-density relationships among a variety of actors within a cluster and they usually express a mutual awareness of a common goal.
- Value chains are more likely to embody bridging ties; but the transformation of bonding into bridging relationships is difficult to develop at the international level and risky to invest in; power asymmetries in global value chains, particularly in buyer-driven value chains, may enable process and product upgrading for SMEs but are unlikely to allow functional upgrading.⁹
- Business associations and regional innovation systems can reinforce the economic impacts of social relations, but they also risk “lock-in” into bonding relationships.
- While building up social relationships is a slow process, particularly when the macroeconomic, social and political context is not supportive, social relations building is sometimes possible even in an insecure and volatile environment with a lack of formal sanctions on opportunistic behaviour.

In the case studies, we have measured social relations and their economic influences through a combination of quantitative and qualitative methods.

⁹ Process upgrading is doing things better, product upgrading is producing better products, and functional upgrading is engaging in additional and higher value-added activities (Humphrey and Schmitz 2000).

Thereby, we have distinguished between economic impacts of social relations (reducing transaction costs, enabling collective action and generating learning spin-offs) and social relations indicators that also include a look at power asymmetries. All the relevant variables, on trust, relatedness and values, were measured in the specific context of each case study, following the suggestion by Swain (2003) to use context-specific qualitative variables.

Our starting point at the micro level was to develop sub-sector maps for the footwear industry in Ethiopia and Vietnam. Such maps show who bargains with whom in particular value chains and visualizes the relative importance of various chains. Following Boomgard *et al.* (1992), we compiled data on types of products produced, price and quantity, as well as the number of firms, producers and traders per value chain. The next step was a stratified sample survey which included questions related to possible power asymmetries.¹⁰ Firms were classified according to firm classifications based on size and level of formality, main market channel served, a characterization of their relationship with their main buyer and type of owner.

Social relations were measured through the trust indicator in the World Value Studies, a proxy for earned and ascribed trust, and a composite trust variable, extent of network participation and associational membership. The economic impacts of social relations were measured as follows: for transaction costs: the share of money and time spent on switching suppliers or buyers, monitoring compliance by transaction partners, and achieving access to production factors; for collective action: cooperation with other producers on information, sharing machines and tools, joint purchase of inputs, joint marketing and joint product development; and for learning spin-offs: improvements made possible by contributions from other local firms, buyers and suppliers, and support organizations. The effect on SME development was measured by performance indicators, such as output, price, quality and growth in employment, as well as by improvements in product and process upgrading. An underlying idea for the data analysis was to investigate to what extent the data on the intervening variables contribute to a better understanding of the relationship between key firm characteristics

¹⁰ A structured questionnaire was used, and Tseguereda Abraham, and Bethel Terefe carried out 52 interviews in Ethiopia and Adam McCarty and Luong Thanh carried out 54 interviews in Vietnam. Peter Knorringa participated in the field work in both Ethiopia and Vietnam, and concentrated on interviewing key respondents in the footwear sector, business association representatives and government officials.

and levels of performance and upgrading. After all, this would be one way to operationalize the significance of social relations in the economy.

For meso-level data, we held semi-structured interviews with key respondents and we carried out a meso-card workshop in both countries with local stakeholders, in which participants put their views, anonymously, on several topics on cards, which were subsequently discussed in the groups. This method helped to bring out the beliefs, interests, norms, and, more implicitly, power asymmetries within the sector. Finally, secondary data from a variety of sources were used in order to get a picture of the macroeconomic, social and political context in which the SME sectors were functioning in each country.

SME Footwear Industry in Ethiopia and Vietnam

Ethiopia. The leather industry in Ethiopia has great potential: the country has one of the largest livestock in Africa and produces high-quality semi-processed leather, used in Italian design handbags and gloves. The major activity in the Ethiopian leather and leather products industry is tanning, and the major tanneries see footwear production only as a spin-off. Footwear is almost exclusively for the domestic market (except for some exports within Africa) where it faces strong competition from Chinese imports. Most footwear entrepreneurs and workers are from the same regional and ethnic background: the Guraghes from around the town of Wolkiso. Since footwear production is largely in the informal economy and does not provide stable employment, most workers are seasonal migrants. Human resources development occurs through a widespread apprenticeship system which reproduces the ethnic and regional concentration, especially in the informal footwear sector. While the small-scale informal sector entrepreneurs and workers face strong competition from cheap imports, the medium scale producers, who produce for higher market segments, face the challenge of moving into exports.

Vietnam. In Vietnam, both the informal and formal footwear sector are booming since the 1990s (as is much of the rest of the Vietnamese economy). Total employment in the informal sector is smaller as compared to the formal sector factories, which are quite large with an often difficult to disentangle mix of private and public ownership. Most workers in the factories are young women. The sector is a significant exporter. Many of the larger export factories are foreign owned, by Taiwanese and Korean multinationals or joint-ventures. The leather is often also imported through

the same Taiwanese and Korean intermediaries who are the primary suppliers to many of the main American and European footwear brands. Hence, the relationship with these foreign owners is crucial. The Vietnamese factory owners and managers mainly take care of organizing the labour force and dealing with government and Party officials. Their success largely depends on political connections, which mainly the larger entrepreneurs possess. Small-scale factories produce both for the export and domestic market, where they face competition from Chinese imports. The medium and large-scale sectors face the challenge of increasing value added by moving from simple assembly into direct exports, which requires them to develop additional skills in designing, marketing and distribution, so that they could wriggle out from under the control over the value chain by the foreign intermediaries.

Firm Characteristics and Market Relations in Ethiopia and Vietnam

In Ethiopia, almost all home-based units (with usually less than five, often family, workers) and even most informal workshops (with typically ten to 15 workers) need to limit production to peak periods in the year, while in Vietnam almost all home-based units and all informal workshops have enough orders to run throughout the year. Within the formal sector it is important to realize that in Vietnam one finds a number of huge processing plants with five or six thousand workers each, which means that one major factory in Vietnam employs more workers than the total employment in the whole Ethiopian footwear industry (which is a bit less than 5,000 workers when one includes the roughly 2,500 persons employed in the informal sector).

Moreover, we have distinguished between the low, main and high end of the domestic market, and a separate category for exports as a main market channel for those firms that have exported at least 50 percent of their production last year. With such a classification, none of the Ethiopian firms qualifies as an exporter. Even though exports are treated as a separate category because of its significance in additional exposure, Vietnamese exporters do not by and large produce higher-quality, higher-price products as compared to those sold in the high-end domestic market. Finally, the main findings on buyer relations were, first, that arms-length relations with buyers are dominant in the domestic market channels, while quasi-hierarchical relationships are dominant in the export channel. Second, network relations appear to be the least common type of relationship with buyers, but occur

more frequently in Vietnam (23 percent) as compared to Ethiopia (10 percent).

Trust

In Ethiopia, there appeared to be no statistically significant relationship between our various trust indicators and firm performance or upgrading (See Table 1).¹¹ In contrast, while also in Vietnam the WVS trust variable was not significantly related to performance or upgrading, our context-specific trust indicator¹² is statistically significantly related to performance (see Table 2). Nevertheless, the general picture shows that variables aimed to measure tendencies in general trusting behaviour are not found to be statistically significantly related to either firm classifications, performance or upgrading (see Tables 1 and 2).

Business Association Membership and Network Participation

In Ethiopia, a new business association for the footwear sector had recently been set up, and it was too early to tell whether it will have a sectoral impact. The strong Vietnamese business associations are intricately intertwined with the government and party apparatus, and reflect a particular mix of networking and hierarchy. While different degrees of more informal network participation by entrepreneurs showed no statistically significant relationship with other variables in Ethiopia, in Vietnam network participation was statistically significantly related with all firm classifications, performance, upgrading, as well as all economic impacts of social capital (see Tables 1 and 2).

11 We have used the Kendal correlation coefficient because our composite variables can be ordered qualitatively in a rather limited number of ordered classes. Therefore, for this data the Kendall correlation coefficient is probably more appropriate than the Spearman rank correlation coefficient because a relatively large number of cases are classified in a relatively small number of ordered classes (Nie *et al.* 1975: 289). Alternatively, Gamma is a measure of association specifically for data arranged into ordered classes (Hays 1968: 844). However, Gamma does not take "ties" into account. To leave out "ties", a frequent occurrence in our data set, means to be left with a more crude measure that relies strongly on a more intuitive interpretation (Nie *et al.* 1975: 228) and which more rapidly takes on higher values. We indeed found that values for both Spearman rank correlation and Gamma were consistently higher than the Kendall correlation coefficient, but that in terms of statistically significant associations no differences were found. To be clear, a Kendall correlation matrix does not imply a direction of causality, but informs us about the extent of association between variables.

12 We asked respondents to what extent they trusted "shoe producers from their own ethnic background", "shoe producers from another ethnic background", "suppliers of inputs", "buyers", "government officials" and, finally, "strangers".

Table 1: Kendal Correlation Coefficients for Ethiopia

	Firm classifications				Social relations characteristics				Social relations economic effects			
	Buyer relation	Market channel	Owner typology	Firm typology	Trust composite	WYS	Ascribed	Earned	Network participation	Transact costs	Collective action	Learning spin-offs
Social relations characteristics												
Trust composite	0.037	0.025	0.177	0.082								
WYS	0.084	0.021	-0.099	0.051								
Ascribed trust	0.433**	0.042	-0.006	0.055								
Earned trust	-0.114	-0.054	0.033	0.105								
Network participation	0.19	0.117	0.113	0.101								
Social relations economic effects												
Transaction costs	-0.153	0.209	0.277*	0.294*	-0.032	0.044	0.011	-0.07	0.05			
Collective action	0.193	0.204	0.122	0.248	0.04	-0.286	0.172	0.046	0.223*			
Learning spin-offs	0.279*	-0.047	-0.075	0.003	0.157	0.086	0.084	0.17	0.179			
Productivity enhancement												
Performance	0.068	0.381**	0.199	0.270*	0.101	-0.072	0.077	-0.109	0.005	0.305*	0.196	-0.044
Upgrading	0.181	0.022	-0.057	0.087	-0.016	-0.070	-0.025	0.076	0.052	-0.245	0.205	0.366**

Source: Authors' calculations. * = 95% level of significance; ** = 99% level of significance.

Table 2: Kendal Correlation Coefficients for Vietnam

	Firm classifications				Social relations characteristics				Social relations economic effects			
	Buyer relation	Market channel	Owner typology	Firm typology	Trust composite	WVS	Ascribed	Earned	Network participation	Transact costs	Collective action	Learning spin-offs
Social relations characteristics												
Trust composite	-0.101	0.016	0.024	0.079								
WVS	-0.226	-0.065	0.065	-0.087								
Ascribed trust	-0.400**	-0.155	-0.403**	-0.366**								
Earned trust	-0.025	0.199	0.132	0.234*								
Network participation	0.462**	0.462**	0.583**	0.615**								
Social relations economic effects												
Transaction costs	-0.365**	-0.591**	-0.537**	-0.472**	0.02	-0.231	0.151	-0.192	-0.346**			
Collective action	0.592**	0.388**	0.556**	0.555**	0.152	-0.066	-0.351*	0.092	0.483**			
Learning spin-offs	0.492**	0.594**	0.669**	0.753**	0.239*	-0.060	-0.317**	0.280*	0.571**			
Productivity enhancement												
Performance	0.434**	0.389**	0.434**	0.439**	0.254*	0.076	-0.305*	0.110	0.420**	-0.374**	0.521**	0.600**
Upgrading	0.451**	0.562**	0.646**	0.636**	0.143	0.031	-0.266*	0.262*	0.546**	-0.516**	0.550**	0.673**

Source: Authors' calculations. * = 95% level of significance; ** = 99% level of significance.

Economic Impacts of Social Relations

The indicators for economic impacts of social relations—reducing transaction costs, enabling collective action and generating learning spin-offs—are all statistically significantly related to our firm classifications, as well as to performance and upgrading in Vietnam but not in Ethiopia. For Vietnam this confirms our hypothesis on the connection between higher levels of economic benefits of social relations for better performing firms, that upgrade more and are relatively larger, and more formal firms that supply more attractive market channels and have tighter relationships with their buyers (see Tables 1 and 2).

Beliefs and Values

The meso-card workshops showed surprising differences between the two cases in respect to the general beliefs and values of footwear producers and other key players in the sector. Whereas, in Ethiopia, only supply-side problems were stressed and cooperation was not prioritized (due to bad experiences in the past),¹³ in Vietnam, demand-side issues were emphasized and cooperation was regarded to be crucial in addressing the key challenge of developing direct access to global buyers. But, the type of cooperation proposed was very hierarchical with an important role attributed to the state.

Bonding and Bridging Social Capital

In both cases we found bonding and bridging ties. Relatively speaking, the Vietnamese footwear sector relied more on a mix of bonding and bridging relationships within the Vietnamese setting and in its relationships with Korean and Taiwanese intermediaries, while in Ethiopia bonding ties were more prevalent. In Ethiopia the main upmarket domestic producers actually also own retail shops through which they sell most of their products, and some of them are also part of a family based business which includes a tannery as a main source of input. A lack of bridging ties in Ethiopia has led these producers to avoid reliance on “market-based” relationships. While

13 This was illustrated with an anecdote from a few footwear producers with export potential who visited a shoe fair in England. They were jointly to develop contacts with potential buyers but the trip was overshadowed by opportunistic behaviour.

this may work within the domestic market, the vertical integration reflex clearly does not help in accessing export markets. Moreover, the bonding relationships in Ethiopia appeared not to help reduce transaction costs or to establish any major form of collective action. Instead, they were limited to very small and often family based networks. Only a few of these family based networks have good access to government, and they will do what is in their power to ensure that other producers remain excluded from such preferential access. In contrast to the Ethiopia case, the Vietnam case shows the potential benefits of bridging ties: it appeared to result in significant positive correlations between network participation, reduction in transaction costs, enabling collective action, generating learning spin-offs, and performance and upgrading. However, the strong hierarchical orientation in the social relations in the Vietnamese footwear sector, reflecting power asymmetries, may be responsible for some constraints such as a difficulty in establishing direct exports. To be able to shift from processors to direct exporters requires the Vietnamese producers, among other things, to engage in building bridging relations with European and American buyers that are both physically and culturally further removed from Vietnam as compared to the Taiwanese and Korean intermediaries.

In the next section we draw some main conclusions from our case studies in an attempt to assess the usefulness of our social economic alternative to social capital.

OLD WINE IN NEW BOTTLES?

In this final section we aim to draw some lessons from our initial attempt to develop a social economic theory of the social relations underlying the problematic notion of social capital. These lessons can be split up in two parts. First, what are the lessons we can learn from unpacking social capital by approaching this from a social economic perspective? And, second, what insights does this alternative approach to economic influences of social relations, in comparison to the mainstream social capital literature, provide for social economics? Let us begin with the first question.

A Social Economic Understanding of What Underlies Social Capital

The approach outlined here substantially differs from the mainstream one, both conceptually as well as empirically. Our case studies have indicated that all three mainstream variables for the measurement of social capital—the

WVS trust question, associational membership, and civic norms—do not appear to be very helpful for an adequate understanding of what social relations *are*, nor for comprehending what they *do* in economic terms.

First, when we asked the WVS trust question, respondents found this by far the most difficult question to answer in our questionnaire. They frequently stated that their response to this question obviously would depend on the type of other person. In other words, they indicated that trust is not simply an individual characteristic or resource, but a value that is established in a relationship, in which it matters who the other is. As a consequence, the general trust indicator appeared not to be statistically significant as a determinant of social relations. We followed the general question up with a more specified set of context-specific trust questions. The composite indicator for trust, based on this set of questions, was, in the case of Vietnam, statistically significantly related to performance.

Second, although context-dependent trust appeared to provide a more meaningful indicator as compared to the WVS trust question in one of the two countries, a more important finding is that our study suggests that trusting *attitudes* are less important in assessing economic impacts of social relations than measuring what entrepreneurs *are actually doing* (in terms of investing in networks, or trying to selectively share and cooperate). In the case of Vietnam, all indicators for the economic impacts of trust are statistically significantly related to performance, upgrading, and to all firm classifications.

Third, the next mainstream variable we used was associational membership, for which we first measured membership of business associations. Again, this appeared not only to be of limited relevance, due to limited formal memberships in one of the two countries, but associational membership appeared also not to be significant. Instead, we measured informal relations through the extent that entrepreneurs actively participated in local networks in each sector. These appeared to be relevant indicators, especially in Vietnam but also to some extent in Ethiopia.

Fourth, rather than adherence to norms, we distinguished between bonding and bridging social relationships. Our case studies confirm the hypothesis that entrenched bonding ties can inhibit bridging relations from developing. Moreover, our case studies underline that for a next phase in development, both in Ethiopia and Vietnam, constructing bridging ties is a key challenge. Certain minimum levels of bonding relationships are a necessary but not sufficient condition to face this challenge. This also requires a more enabling environment for private-sector development, an environment that lowers *macroeconomic* uncertainty and volatility, and with credible sanctions on opportunistic entrepreneurial behaviour.

Fifth, we added the dimension of power asymmetries to our measurement of social relationships. These power asymmetries appeared to play a not unimportant but rather complex role. The Vietnam case clearly showed how control by others over a value chain constrains firm upgrading, and that exclusion from political alliances prevent small-scale entrepreneurs to become more successful. The Ethiopian case showed static benefits of ethnic and regional concentration in the footwear sector in terms of access to domestic buyers, suppliers and human resources. But these bonds were also likely to be responsible for dynamic disadvantages: the strong ethnic bonds within the informal sector may press for sharing the little earnings, rather than investing these. In the small formal sector the main family based groups fight each other for good access to government and try to go it alone in the international market, which is a self-defeating strategy given their small size by international standards.

Finally, the above conclusions lead to a main conceptual point. They suggest that social relations cannot be regarded as an individual characteristic or resource, that it is better not measured by the WVS trust question, formal group membership or civic norms, and that it is affected, positively and negatively, by power asymmetries. In macroeconomic terms, this suggests that social relations cannot be reduced to a single independent variable next to a set of common economic variables in a growth equation, as is common in the mainstream approach. Instead, social relations are likely to affect every single other economic variable in a production function as a productivity scale factor for each individual production factor, representing the (in)efficiency impact of context-specific social relationships. This observation is also in line with our working definition of social capital, which stressed how social relationships influence both access to and productivity of economic resources. Moreover, this feature of the causality of social capital is in the alternative social capital literature sometimes more loosely referred to as “lubricant” (Field 2003: 63), or “social cement” (Repetti 2002) in economic interactions, influencing the efficiency of these interactions, partly through intended actions such as collective action, and partly through externalities from social relations.

What Does this Contribute to Social Economics?

The second question to be addressed here concerns the question whether there is any value added from our suggested alternative approach to social capital for social economics in general. We do think that there may be some

value added, although this research is still very tentative and much needs to be explored yet. What we found illuminating in our struggle with the mainstream literature and subsequently, doing our empirical case studies through a trial-and-error process of developing alternative indicators and detailing social relationships, was the many ways in which it appeared feasible—some ways we followed, others not—to do empirical research on economic impacts of social relationships in a largely non-instrumental way. We did not need utility functions, nor assumptions that entrepreneurs always act in their self-interest. We did not have to picture functionalistic relationships in statistical equations but could instead get some basic picture of meso-level interactions between actors, including their beliefs and values. In other words, it appeared possible not to simply make assumptions about agency and types of relationships, but to actually picture, measure, interpret and intuitively understand, at least to some extent, the complex relationships between social relations and economic performance in a particular sector of the economy, in two widely differing country contexts. What we found was not just that relations matter, but *how* they matter, in a substantive way, not by referring to a black box variable of social capital, but by unpacking this into types and extent of social relations, specific intended and unintended economic impacts, and subsequent effects upon firm success. Of course, our case studies are merely some incomplete examples, from which no strong conclusions can be drawn. But we think that such an alternative to social capital, drawing on social economics, is a bit more than old wine in new bottles: it may well offer some concrete, contextual methodology for social economics for the study of meso-level phenomena, in which transaction costs, collective action, and learning spill-overs play a role.

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