Trust, Distrust, and Power

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The so-called “encapsulated interest” account of trust, developed by Russell Hardin together with other interested scholars, draws together an important body of thought about trust and its meaning in social and personal relations.[1] Trust, under this account, involves considered expectations about the interests of others to behave in a trustworthy manner. Some scholars argue that trust of this sort is not trust at all. Laurence Becker (Becker 1996), for example, argues that “cognitive” trust, of the sort discussed in the encapsulated interest account, is indistinguishable in the final analysis from knowledge and power. Becker over-simplifies considerably; it is clear both that many instances of power over another, or knowledge of another’s interests, do not create trust, and that even when power may engender trust, the concepts remain distinguishable. For example, as Hardin argues (Hardin forthcoming), trust does not apply in a relationship where I am holding a gun to your head; while I certainly have power over you, and know that you have an overwhelming interest to do what I tell you to do, the degree of certainty that I have about your interests renders trust irrelevant. While power, and knowledge of the effects of power on interests, may clearly affect trust under certain circumstances, the concepts should not be conflated.

This said, the relationship between power, trust and distrust in the encapsulated interest account remains to be fully explored. Under some circumstances, power seems to drive trust out. When I have a gun to your head, not only is it difficult to describe my relationship to you in terms of trust, but also, quite obviously, it is nearly impossible for you to trust me. When I hold such power over you, there is no reason for me to take your interests into account.[2] At the same time, trust clearly must sometimes be possible between actors of unequal power. Otherwise, the concept’s applicability is confined to a relatively small set of human relationships; those between genuine equals.

Thus, an account of the relationship between trust (under the encapsulated interest account) and power, should fulfil two criteria. On the one hand, it should account for the difficulties of maintaining trust in a situation of extreme disparities of power between actors. But on the other hand, it should be able to accommodate trust in relationships where disparities of power between actors exist, but are less marked. Clearly, it must thus be able to distinguish between those social situations in which power drives out trust (and often leads to distrust) and those situations in which power and trust are not mutually exclusive.

In this paper, I canvas one set of arguments which draws such a distinction. The literature on credible commitments, which shares much common ground with the encapsulated interest account of trust, discusses the need to "tie the king's hands" in certain instances (North and Weingast 1995; Miller 1992). Certain actors may be too powerful to be trusted - they have no incentive not to renege on their commitments. However, their power may not actually serve their interests - because they cannot be trusted, other actors will seek, as much as they can, to avoid dealings with them that require trust. Thus, as North and Weingast argue, the ability of the early modern British state to raise monies was greatly increased when its power to break its commitments was curbed. Creditors could lend money to the government in the reasonable expectation that they would have it returned, with interest. North and Weingast seek to use this train of reasoning to draw general lessons for political economy; however, their arguments also provide a basis for arguments about the relationship between trust, distrust and power.

As I seek to show in this paper, one can plausibly maintain that under the encapsulated interest account of trust, one's relationship with another actor may involve trust, even if that actor is more powerful than you, *up to the point where that actor is so powerful that she is no longer capable of making credible commitments to you*. Before this point is reached, power and trust are not mutually exclusive; while disparities in power may certainly affect the way in which the proceeds of trust-based cooperation are distributed, they will not necessarily prevent trust from arising. After this point, it is difficult, if not impossible, to use trust to describe your relationship with another, who is so powerful that they cannot make credible commitments to you. If you are so much more powerful than me that you are no longer capable of giving credible commitments, then it follows that our relationship is insufficient to bind you to act in my interest. I will have no reason to trust you, and in many circumstances will actively distrust you. This further means that insofar as I have no reason to trust you, you will have no reason to trust me. I lay out the reasoning behind this argument in the next section.

The paper begins with a section which briefly lays out the encapsulated interest account of trust, and how the logic of credible commitments may be accommodated within it, thus setting out a basic account of the relationship between trust, distrust and power. It then goes on to examine the relationship between trust and power in a specific setting; that of trust between business actors in inter-firm relationships. It shows that both trust and power differentials between actors have consequences for these relationships. Moreover, by paying proper attention to how power disparities affect the ability to make credible commitments, one can explain otherwise anomalous behavior on the part of business actors.

Incorporating Power into the Encapsulated Interest Account of Trust.

The "encapsulated interest" account of trust, as set out by Russell Hardin, argues that trust involves expectations about interests (Hardin forthcoming).[3] I trust you to the extent that I believe that you have an interest in fulfilling my trust. Trust is not diffuse - it is likely to be limited to a particular matter (or matters); A trusts B to do X, but she may not trust B to do Y. Trust is an expectation, but it is a quite particular sort of expectation; it involves A's expectations on the basis of B's specific interests with regard to her. As Hardin argues, it follows that trust is a *relational* concept. This is to say that it depends on the specific relationship between A and B; A's trust of B usually depends on their relationship, and the interest which the relationship creates for B in behaving in a trustworthy fashion.[4]

This suggests how the encapsulated interest account might incorporate power. Power, like trust, is a notoriously difficult concept to pin down; here, I follow Jack Knight, who argues that "to exercise power over someone or some group is to affect by some means the alternatives available to that person or group." (Knight 1992, 41). Knight goes on to argue that a good index of power in bargaining situations is the set of alternatives faced by a party in the case of breakdown. Parties which have many possible attractive alternatives should a particular relationship not work out, will be more powerful than parties which have few such alternatives, because they can more credibly threaten to break off bargaining, thus affecting the other's feasible set. Power, under this definition, is clearly relevant to trust. If I am capable of affecting the set of feasible actions which you may undertake, I have influence over your ability to pursue your interests. This may affect your trustworthiness with regard to a particular matter - you have to take my interests into account.

Viewed in this way, power is clearly relevant to the encapsulated interest account of trust (although I wish to re-emphasize that the terms power and trust should not be conflated, and that extremes of power do not translate into extremes of trust). Merely re-describing trust relations in terms of power does not tell us very much. However, examining the relationship between power and trust may lead us to two interesting conclusions. First, power may affect trust insofar as it touches on parties' evaluation of the relative worth of the relationship.

Second, to the extent that power affects the possibility of trust and trustworthiness, it also may affect the kinds of cooperation that take place on the basis of trust and trustworthiness.

The first point follows more or less clearly from Hardin's emphasis on trust as a relational concept. As Hardin puts it,

> I trust you because I think it is your interest to attend to my interests in the relevant matter. This is not merely to say that you and I have the same interests. Rather, it is to say that you have an interest in attending to *my* interests because, typically, you want our relationship to continue. (Hardin, forthcoming, page number unknown)

It may be in your interest to behave in a trustworthy fashion because of the economic benefits flowing from our relationship, or, in thicker relationships, because of the non-material benefits that you receive from it. In both cases one might say that your interest in being trustworthy is affected by my power to break the relationship, or to redefine its terms to your disadvantage, should you behave in an untrustworthy fashion. If one party wishes to continue the relationship, and the other party values it more lightly, and further has scope to affect the relationship to the first party's advantage or disadvantage, that second party may be said to have power over the first. In many circumstances, the parties in a relationship will have roughly symmetrical power; neither will want to break or alter the relationship very much more than the other. In such circumstances, power will not be especially relevant to explanations of the existence and form of trust. However, substantial asymmetries may exist, even in "thick" relationships, which carry a considerable emotional weight. In the presence of such asymmetries, power may have an important impact on trusting relationships. To the extent that one individual has many possible attractive alternatives to a given relationship, that relationship will be less valuable to the individual in question. The other individual in this relationship may not have so many alternatives, and thus be more dependent on the continuation of the relationship.[5]

This conclusion leads to the second point; that asymmetries in power are one source of asymmetries in trusting relationships, and thus in the forms of cooperation that take place on the basis of trust in these relationships.[6] If asymmetries of power exist, they are likely to have an impact on trustworthiness, and thus on trust. When I have many attractive alternatives to my relationship with you, and I know that you have very few, I may be more inclined to take advantage of you in some circumstances. This may happen in "thick" relationships as well as in thin ones; everyday life provides evidence, for example, of friendships where one party is considerably more socially "attractive" than the other, and treats his or her less fortunate acquaintance badly. Power asymmetries may play an important role in family relationships too, as Brown (this volume) vividly demonstrates. This said, if relationships involve genuine emotional attachments they are less likely to be highly asymmetrical in this sense; both parties may have sunk considerable resources into the relationship, and will be unwilling to abandon it lightly.

Thus, power may affect trust and trustworthiness insofar as it impinges on a relationship which both parties value. If one party values the relationship more lightly than the other (perhaps because of the existence of other, potentially attractive relationships for the first party), she may be said to have power, in the sense that she can affect the set of feasible actions available to the other by credibly threatening to end the relationship, in order to redefine it to her advantage. Trust remains possible in such relationships; to the extent that both parties attach some value to the continuation of the relationship, they both have some reason to take the other's interest into account, and thus to behave in a trustworthy manner. The point is that such trustworthiness (and trust) may be asymmetrical; insofar as one party values the relationship more lightly than the other, she has less need to be trustworthy in order for the relationship to continue. If A values the relationship less than B, A may still trust B over a wide range of issues (or over more important issues), but B may only be able to trust A over a narrower (or less important) range. While B may distrust A over many issues, he may prefer to continue the relationship, given his alternative options, provided that the relationship still offers some overall benefit to him.

Encapsulated Interest and Credible Commitments

The previous section has sought to establish that trust may co-exist with asymmetries of power under some circumstances. This, however, leads to a troubling question. If, as Hardin has argued, trust is not present in relationships involving extreme disparities of power, what is the point at which power asymmetries change their causal weight, so that they no longer merely affect trust relations, but instead make them impossible? Here, I wish to point to similarities between the debate about trust in relationships between individuals, and the ongoing debate in political economy about the role of the state. While I do not want to gloss over the very important differences between these two levels of analysis, political economy provides important lessons that may (with some care) be applied to trust between individuals.

The power of the state, and its implications for relations with society, has been an important question for political economists and economic sociologists since the foundations of the two disciplines. Some scholars, especially paternalist conservatives, have held that an absolute ruler may be trusted to rule for the common good, because his particular interest is commensurate with the general interest. Gibbon, for example, in his account of the reign of Septimus Severus, makes the claim that

> The true interest of an absolute monarch generally coincides with that of his people. Their numbers, their wealth, their order, and their security, are the best and only foundations of his real greatness; and, were he totally devoid of virtue, prudence

> might supply its place, and would dictate the same course of conduct. (Gibbon 1995, 95).

However, most social science suggests the opposite, finding that the non-accountability of the ruler to other social actors has negative consequences for general welfare. Weber (1978), for example, distinguishes between Oriental and European varieties of feudalism. In the former, the ruler had absolute power over his nobles, granting and taking away authority from functionaries at whim. In the latter, the monarch granted land in return for military services, creating a complex web of reciprocal obligation (fealty) between monarch and liege-lord, which constrained the former and was crucial to the later development of the rule of law, and the economic development of the West. Most recently, a body of scholarship associated especially with Douglass North (1981) and Margaret Levi (1988) has clarified the often fraught relationship between state and other actors in the sphere of economic development.

It is not difficult to show that this work is relevant to the relationship between trust and power. It asks whether, under what circumstances, and to what extent, very powerful actors (state actors) may take the interests of less powerful actors (typically the general public or economic agents) into consideration, or, in a very broad sense, when more powerful actors may be expected to be trustworthy towards weaker ones. Nowhere is this clearer than in North and Weingast's work on "credible commitments" and the Glorious Revolution (North and Weingast 1995). These authors argue that the degree to which the sovereign is himself bound by the rules governing commercial exchange is crucial to the development of markets. In early Modern Europe, sovereigns were not necessarily bound to repay the debts that they had incurred; they could repudiate them at will. Their power to do this was not necessarily to their advantage; it made merchants unwilling to advance them loans. Because they were unconstrained by law, they had difficulty in making credible commitments. North and

Weingast note two possible solutions to this problem. Monarchs could establish a reputation for repaying debts, which could become a valuable asset (Kreps 1990), providing them with an incentive to repay, and thus reassuring merchants that they were trustworthy. This solution was impracticable in early Modern Europe, where states were frequently at war with each other, so that the temptation for the sovereign to renege was often overwhelming. Alternatively, the crown could itself become subject to the law. The Glorious Revolution, and the departure of the Stuarts, saw the British crown becoming subject to legal and institutional constraints, but simultaneously becoming vastly more credible to lenders, so that the level of public debt grew fifty-fold between 1688 and 1720.

The problem faced by the British crown - that it was too powerful to give credible commitments easily - can be generalized to many other social situations. Gary Miller has shown the relevance of this problem to the political economy of the firm (Miller 1992, 2001). Many aspects of the internal hierarchy of the firm, from piece-working to deferred compensation of workers, require that the owners of the firm credibly to commit *ex ante* not to take *ex post* advantage of workers, even though opportunism would be to their immediate benefit. The hierarchical advantage enjoyed by owners and managers means that it is difficult for them to make these commitments - to do so, they have to constrain themselves, either through creating an appropriate "culture," or through creating a firewall between shareholders, whose interest is in short term profit, and managers and directors, who ideally should have a longer term perspective, and be prepared to make the necessary commitments over time. Only through these means can the stakeholders in a firm coordinate on an efficient equilibrium (or at least an equilibrium that is superior to the never trust/never honor trust equilibrium which strictly dominates the one-shot trust game).

These arguments provide the basis for two important conclusions. First, one may identify conditions under which asymmetries of power will almost certainly prevent trust from arising, and will lead to distrust. A certain degree of asymmetry in power may be tolerated in a relationship, although it is likely to have distributional effects. But if I am so powerful that I may renege without significant consequences, you may reasonably doubt my interest in continuing the relationship; my most attractive option may be to abuse your trust. In other words, I am incapable of making credible commitments to you; commitments that you know it is in my interest to fulfil once I have made them. To say that I am incapable of making credible commitments to you is to say (among other things) that you are incapable of retaliating effectively should I betray your trust. The hurt that you can inflict by breaking off your relationship with me is potentially outweighed by the benefit I would receive from abusing your trust. Furthermore, it is to say that there is no reason external to our relationship for me to behave in a trustworthy manner within it. To put it another way, the point at which I am so powerful that I can no longer make a credible commitment to you is just that point when I am so much more powerful than you that you can no longer trust me.[7]

Clearly, under circumstances where you cannot trust me, you will avoid relationships with me that require trust. You will rationally distrust me, and expect me to take advantage of you at every opportunity, so that you are unlikely to benefit from any such relationship. But, even in the unlikely event that you were to engage in such a relationship (you were somehow coerced), I would probably be unable to trust you either. The relationship provides you with no good reason to behave in a trustworthy fashion, because you know that it provides me with no good reason. To the extent that you cannot expect me to be trustworthy, your particular relationship with me has no value, so that (all other things being equal) you will not be trustworthy either, and I will not trust you. You are likely only to "cooperate" to the extent that you are forced to.[8] Extreme disparities of power mean that both the stronger and weaker actors will have good reason to distrust each other.

Second, however, this literature points to the existence of a gray zone, in which asymmetries of power are not so great as to lead inevitably to mutual distrust, but may significantly hamper the development of trust. As the more general literature on trust and trustworthiness emphasizes, trust invariably involves some degree of uncertainty; one can never fully divine another's interests, and thus one can never be entirely sure that another will behave in a trustworthy manner, although one may have reasonable expectations. Where there are substantial (although not overwhelming) asymmetries of power, such uncertainties may have important consequences. The less powerful actor may be unsure whether his relationship with the more powerful actor gives the latter sufficient reason to behave in a trustworthy fashion. As Kramer (this volume) argues, social psychology provides us with good evidence that less powerful actors will often misconstrue more powerful actors' intentions, interpreting them in the worst possible light. In these situations, even where the more powerful actor genuinely wishes to behave in a trustworthy manner, she may have difficulty in persuading the less powerful actor of her good intentions. Even where the latter does not fall victim to the kinds of paranoid cognition that Kramer identifies, he may be unsure as to the interests of the former in borderline cases. Furthermore, he may reasonably worry that even if the more powerful actor has an interest in behaving in a trustworthy fashion now, circumstances may easily change so that it is no longer in her interest to be trustworthy in the future.

North and Weingast (1995) and Miller (2001) discuss the implications of such uncertainty.[9] First, actors may have variable time horizons. A monarch may wish to borrow money, and may be willing, most of the time, to commit to repay her debts; the shadow of the future may loom long enough to give her reason to be trustworthy. However, her time horizons may shift rapidly if war threatens, so that she has a strong, and perhaps even overwhelming interest in defecting in order to avoid extinction. A potential lender, knowing that there is a substantial chance of war (which may not be quantifiable so as to transform uncertainty into risk), may be unwilling to advance money, however sincere the monarch may appear. A similar logic may apply within firms, where owners' commitments to reward their workers are rendered less credible by the possibility of economic downturn, when they will have a strong interest in reneging. Creditors and workers, knowing that wars and economic downturns are not extraordinary events, will often be disinclined to believe the promises of kings and owners that they will give full return over time.

Second, and more profoundly, many problems of trust may be treated as problems of equilibrium selection in an infinitely repeated game, where actors may be uncertain of each other's ultimate intentions (Miller 2001). Here, asymmetries of power may make it more difficult to coordinate on a mutually beneficial equilibrium. One or both actors may have a strong incentive to renege in the short term. If there is uncertainty that one actor will play an honorable strategy, then the other actor must always worry that the first actor will violate trust, thus making it more difficult for both to converge on a mutually beneficial equilibrium. The most obvious solution to this problem is for one or both of the actors to make a binding commitment that they will behave honorably. However, if one of the actors is very much more powerful than the other, it will be difficult for her to make that commitment. She will have difficulty in using the relationship as surety for good behavior insofar as there are other attractive options for her. Even when she genuinely desires to cooperate, she may have difficulty in convincing the weaker actor to extend the necessary trust for cooperation. In order to remedy this problem, Miller's logic suggests that she is best advised either to establish an appropriate “culture,” which may be linked to reputational sanctions (Kreps 1990), or to subject herself to external institutions or organizational forms which make it difficult or impossible for her to abuse trust.[10] By pursuing either of these courses she is constraining herself, and limiting her future ability to exercise power, in order to convince others that she will not use that power to traduce their trust. Brown (this volume) provides a detailed analysis of how a more powerful actor may pursue a strategy that both limits his power and serves as a token of future intentions. She discusses how both a Madagascar villager and his younger siblings may prefer to undertake certain transactions on the basis of cash rather than more informal means of exchange; this limits both the elder brother’s ability to abuse his greater bargaining power, and reassures his siblings of his future good intentions. Levi, Moe and Buckley (this volume) discuss how external institutions may at least alleviate distrust between actors with asymmetric power, even where they do not necessarily create trust. However, they also demonstrate that such institutions have their own costs, and may be captured over time by more powerful actors. These quandaries are beyond the scope of my discussion.

Thus, in this and the previous section, I have sought to show that trust may be affected by power: power asymmetries impinge on the value of the relationship between the trusting and trusted parties. Relationships involving trust may be asymmetrical - I may trust you with matters over which you do not trust me, and vice versa, and one important source of such asymmetries is likely to be differences in power between individuals. To the extent that I have many other options outside our relationship, and you do not, I may have less reason to behave in a trustworthy fashion towards you; the breakdown of our relationship (when you accuse me of untrustworthy behavior) is likely to hurt you more than it hurts me, and we will both know this. Our relationship may still be characterized by trust - but I will probably be able to trust you over a wider range of matters than you can trust me.

However, at a certain point, power asymmetries can become so marked as to drive out trust. When one actor is very much more powerful than the other, she does not have to take the other's interests into account. Thus, she has no reason to be trustworthy, and is incapable of giving credible commitments. Further, one can extend the argument to say that the less powerful party has no interest in being trustworthy either. Extreme disparities of power are likely to give rise to mutual distrust.

Thus one can distinguish between situations where asymmetries of power exist, but are not so marked as to prevent trust, and situations where such asymmetries are so pronounced that they make credible commitments (and trust) impossible. One may also identify an intermediate area at the cusp between these two, where uncertainty means that the less powerful actors are unsure as to whether power disparities and interests are such as to make trust impossible or not. Here, if the more powerful party wishes to create the possibility of cooperation, it behoves her to constrain herself in such a way that her power to defect is lessened, so that others may reasonably trust her (or, at the least, have less reason to distrust her).

Trust, Distrust and Relations between Firms.

The relationship between power, trust and distrust that I have described is likely to apply to many areas of social life, including economic relations. More particularly, it may help to explain subcontracting relations between firms. At first glance, such relations might appear to involve institution-induced expectations, rather than trust; indeed, Oliver Williamson argues that the concept of trust has little purchase on economic relations

(Williamson 1993). However, institutions, whether they be formal laws or informal social rules, will not fully determine outcomes in real-life situations, providing scope for quite rich varieties of trust (and distrust).[11] Very frequently, subcontracting relations involve quasi-personalized relationships between individual actors of the sort emphasized in the encapsulated interest account. Furthermore, these relationships provide a good test case for the argument that power affects trust relationships. Such relationships do usually involve imbalances of power; typically (although by no means universally), the final firm making the order has more options, and thus more power, than the subcontractors. If the theory which I have outlined in the previous section has empirical merit, and if the power imbalances between final firms and subcontractors are indeed substantial, final firms will face a difficult balancing act. On the one hand, their power may allow them to shape long term relationships with subcontractors to their particular advantage. But on the other hand, they may run the risk of finding themselves too powerful for their own good; to the extent that subcontractors have difficulty in trusting them, final firms may be incapable of reaching cooperative equilibria where both parties would benefit. In order to examine the potential relevance of power to choices made by actors, and to their outcomes in terms of trust and cooperation, I turn to three examples drawn from the literature on "thick" subcontracting relationships; Japanese subcontracting practices in the weaving industry, relations between metalworking firms in France, and relations in the packaging machinery industry in Italy.[12]

Weavers in Japan

Much of the recent literature on subcontracting relations has focused on Japan,[13] even if the Japanese model of industrial organization seems less successful than it did a decade ago. Many of the key arguments about Japanese subcontracting practices were set out in a classic article by Ronald Dore (1992), on "goodwill" in the Japanese economy. Dore wishes to argue against classical and neo-classical economics' persistent skepticism about economic behavior that is not motivated by self-interest. As a counter-example, he proposes the existence of trading relations between economic actors in Japan, which he sees as involving "moralized trading relationships of mutual goodwill" (Dore 1992, 163). In Dore's argument, such relationships have important economic benefits; they lower transaction costs and decrease the likelihood of opportunism. In addition to making certain kinds of coordination and "X-efficiencies" available, relationships of goodwill make it easier for economic actors to trust each other.

Dore turns to the fragmented Japanese weaving industry for evidence of goodwill in practice. Weaving in Japan relies extensively on subcontracting relations where "weavers," who own the automatic looms, produce for "converters." Typically, smaller weavers are monogamous - they tend to produce for only one converter - although larger weavers may have relationships with three or four converters. Dore suggests that relationships between these firms does not involve the kinds of open confrontation found in many Occidental trading relationships, where bargaining is seen as a zero-sum game. Instead, both sides of the relationship recognize a moral obligation to try to maintain the relationship. When the relationship breaks down, it usually involves one or both of the parties making accusations of "insincerity." A similar logic of relations is found within the larger *grupu* - which involve stable, obligated bilateral trading relationships between large firms (Dore 1992) - as well as in the Japanese economy more generally, where survey evidence suggests a widespread reliance on long term relationships involving trust between economic actors (Sako 1991).

"Goodwill," as Dore defines it, is clearly closely connected with trust, a connection made explicit in Mari Sako's (1991) portmanteau term, "goodwill trust." What is noteworthy is that Dore's "goodwill" relations seem to involve substantial imbalances of power. Dore argues that weavers are more dependent on converters than vice-versa, so that the converter is in a position of hierarchical superiority. There are many weavers, each in competition with each other, and relatively few converters. This has implications for how the benefits of cooperation are distributed. Especially in hard times, the weavers may find their profits squeezed by the converters (Dore 1991). More generally, the converters have less need to behave in a trustworthy fashion towards weavers than weavers do to converters. Weavers with verbal contracts are more likely to have their goods returned for quality deficiencies than weavers with written contracts. Furthermore, such returns curiously become more common when prices are falling, so that a rejected lot can be replaced with a newly contracted, cheaper one. Dore finds that the weaker partner has to show considerably more "sincerity" to the more powerful partner than vice-versa.

However, as Dore is keen to emphasize, even if these mutual obligations are asymmetrical, they are not one-sided. Although converters may take advantage of weavers, they do so within certain limits. Both the losses of bad times and the profits of good times are shared, even if in an unequal fashion. Furthermore, the converter is expected to refrain from using his superior bargaining power to push weavers to the verge of bankruptcy. His obligation not to do so (as well as the obligations of the weavers to show sincerity) is reinforced by reputational mechanisms (Dore 1991).

As should be immediately apparent, the kinds of subcontracting relationship identified by Dore in Japan may very easily be recomposed in the terms of the simple theory of trust, distrust and power that I have outlined in the first section of this paper. Subcontracting relations between converters and weavers clearly involve trust. Economic actors find themselves bound into long term relationships, so that each partner may reasonably believe that the other partner has an interest in behaving in a trustworthy fashion in order to continue the relationship. However, converters have many more weavers with whom they can potentially do business than weavers have converters. Because converters have more options outside the relationship, they have more power inside it too. This translates not only into an asymmetrical division of the benefits of cooperation, but into differences of trustworthiness and trust. Converters can behave in an openly untrustworthy fashion in some aspects of the relationship without causing it to fail; weavers typically cannot. This said, while the asymmetry of power between converters and weavers is enough to shape their relationship, and the forms of trust it involves, it is not enough to prevent trust from arising in the first place. Converters are restrained by reputational mechanisms, and quite possibly by social norms, from using their power to reshape the relationship so that weavers derive no benefit from it (and are potentially driven into bankruptcy).[14] Weavers can thus rationally trust converters, at least over some matters, even if converters may sometimes take advantage of them.

Machine production in France

The quandaries of power may also help explain a puzzling finding reported in the literature on subcontracting; that final firms may tend to discourage subcontractors from becoming too dependent on them. Perhaps the most developed account of this phenomenon may be found in the work of Edward Lorenz (1988, 1993, 1999) on trust between machinery producers in the Rhône-Alps region of France. Lorenz finds that technological changes had led these firms to adopt new forms of production, and in particular to decentralize productive activity. Certain standardized stages of the production process, which had previously been carried out in-house, were put out to smaller subcontractors. As in Japan, relationships between final firms and subcontractors involved trust between the relevant economic actors.

Lorenz's interviewees described their relationships in terms of partnership, loyalty and trust. Because the production process might involve unexpected contingencies, neither institutional enforcement nor reputational incentives could provide a sufficient basis for cooperative relations on their own (Lorenz 1993, 1999). Instead, so called "moral contracts" (*contrats moraux*), that involved basic procedural rules for how unexpected events might be handled, provided the basis for cooperation. These moral contracts did not necessarily involve genuine emotional or normative commitments; while business actors spoke of their commercial relations in terms of friendship, this language was intended to coordinate expectations (in situations of difficulty, actors should behave "as if" they were friends) rather than to express deeper forms of commitment. In Lorenz's (1988) lapidary phrase, business actors were "neither friends nor strangers."

Lorenz's evidence indicates that these firms sought to diversify their relations in order to mitigate the risks of undue dependency. Final firms would solicit tenders from at least three subcontractors before engaging in a relationship, and preferred to split orders between a minimum of two, so that they could switch to one if there was a problem with the other. More unusually, not only did final firms seek to avoid becoming dependent on particular subcontractors, but they actively sought to discourage subcontractors from becoming too dependent on them. The final firm and the subcontractor sought to create a partnership where the final firm would account for no less than 10% and no more than 15% of the total output of the subcontracting firm. Less than that meant that the subcontractor did not have enough reason to take account of the particular needs of the final firm, while more meant that the subcontractor would become unduly dependent on the final firm, so that it would be crippled if the final firm ran into serious difficulties.

The interesting question is why final firms would encourage a situation in which subcontractors did not become too dependent on them, given Lorenz's assertion that they did not possess genuinely other regarding motivations. Why should decision makers within the final firm care enough about the possible effects of their own economic difficulties on others, so that they were prepared to discourage these others in advance from becoming too dependent on them?

One may plausibly argue that the reason for this behavior lies in the dilemmas of power discussed in this paper.[15] If final firms wish to encourage genuinely cooperative relations with subcontractors, they may have good reason to ensure that power disparities do not prevent this. If a subcontractor becomes overly dependent on a particular final firm, then the owners of the subcontracting firm have greater difficulty in trusting the decision makers in the final firm not to renege on informal commitments by pocketing the additional effort given by the subcontractor without rewarding it in turn. Trust may be especially difficult in times of economic hardship, when the final firm may face an overwhelming temptation to defect by using its power to squeeze the subcontractor for short-term profits. If the owners of subcontracting firms know that difficult periods are likely at some point in the future, but are unable to predict when, it may be difficult for them to enter into a genuinely trusting relationship with the final firm. Under these conditions, it may be wise both for the final firm and the subcontractor to create a relationship where trust is possible (both have a sufficient stake in the relationship for trust to arise) but where the subcontractor does not become unduly dependent on the final firm (for fear that this dependency might tempt the final firm too much). The arrangements reached by firms in Lorenz's case study seem designed as compromises between these two exigencies.

Packaging Machinery Production in Italy

Finally, one may turn to a case in which power relations are currently changing, the packaging machinery industry of Bologna, capital of the Italian region of Emilia-Romagna.[16] Packaging machinery manufacturers and subcontractors are both located in a relatively well-defined geographic area, “Packaging Valley,” where there has historically been a high degree of cooperation in the production process. Indeed, production is radically disintegrated, so that final firms tend only to carry out sales, design, and assembly of the final product. The actual manufacture of individual parts and components is carried out by subcontractors, working to designs provided by the final firms. This extraordinary level of vertical disintegration is typical of Italian “industrial districts,” in which cooperation between a multitude of smaller firms has typically served as a substitute for hierarchical production within the firm (Brusco 1990). There must be extensive trust between final firm and subcontractors, if the risks of exploitation (on the part of final firms) and hold-up (on the part of subcontractors) are not to prevent cooperation. This trust is possible because of informal institutional rules at the local level, which provide for a high level of honesty in personal dealings, and the sanctioning of firms which behave opportunistically (Farrell 2001, Farrell and Knight forthcoming). These rules have permitted a set of understandings to come into being, which have themselves become institutionalized, in which final firms commit to providing work over time in exchange for the subcontractor’s flexibility and honesty. However, as in many other Italian industrial districts, power relations between firms are shifting in a manner which has important implications for trust and cooperation.

Two sets of relationships are important here - relationships among final firms themselves, and relationships between final firms and subcontractors. Final firms in the packaging machinery industry were traditionally highly specialized. Each firm might specialize in machines for a particular stage of the packaging process in a particular industry. For example, one firm might produce dosing machines that filled gelatine capsules with a drug for the pharmaceutical industry, whereas another, quite different firm, might produce the machines that packed these gelatine capsules in blister-packs. Thus, several different final firms might come together to provide the machines for the packaging line ordered by a customer firm.

Increasingly however, larger firms in the industry have bought out smaller firms, so that they can provide a complete line of machinery. This is driven by customer demand - large firms in the pharmaceutical and food industries no longer wish to deal with several smaller firms, instead preferring to create closer ties with a single supplier of packaging machinery, that can provide all their needs. As large final firms buy out their smaller counterparts, they assume ever-increasing control over the packaging machinery district. Because of their strong relationships with their customers, they have no reason to fear competition from smaller firms, which are increasingly hierarchically subordinated. As described by the managing director of one of the largest firms in the district;

> in this field we exist really, when we have the control of the final customer. In manufacturing of industrial or capital equipment like this, if you manufacture capital equipment you have got to have the grip on the customer yourself. What you could say is that there is a space for a small company, but they will supply mostly through the sales organisations of larger companies. That means they are nothing, they can be purchased easily, or destroyed or eliminated. Because the market here is not for this machine, it is for these customers, and if you don't have these customers, you don't exist. You have got to have these customers to exist.

Thus, the district is increasingly becoming dominated by a small number of final firms, which are buying up most of their competitors. This has knock-on consequences for the relationship between final firms and subcontractors. Previously, subcontractors in the district had considerable latitude in their relations with final firms. While there were many subcontractors in competition with each other, there were also many final firms which they could work for. The result was a situation of rough equality in bargaining between final firms and subcontractors; both had many alternative options if they failed to reach agreement in a particular set of negotiations. Now, in contrast, there are rather fewer final firms that subcontractors can work for. The result is an increase in hierarchy. Final firms, which face the demand for ever higher quality from their customers, seek to bring this through by hierarchically organizing their subcontractors in a "Christmas tree arrangement" in which the final firm is at the vertex, certain key subcontractors, which organize the production process beneath, and a large number of smaller subcontractors who report to the "key" subcontractors at the next level. Final firms have more power over their subcontractors, which they may use to extract concessions (such as greater flexibility) without providing the quid pro quo (guaranteed levels of work in the long run) which had previously been given. A senior manager in another large firm in the district describes how they have built up dependent subcontractors, which rely on the firm for up to 80% of their turnover, but have to sign up to terms which are "very favorable" to the final firm, without any guarantees of future income.

> We ask for a lot of flexibility from our suppliers! That is the main concern they have normally. They don't like to be treated in that way, because for us it is difficult to predict what is the workload that we would pass to our suppliers. So normally our projection is always pretty wrong. But on the other side, for them we are very important. So they just complain.

Here, final firms, unlike their counterparts in Rhône-Alps, are deliberately re-organizing their relationships in such a way as to emphasize power over trust. It remains to be seen whether this strategy will be successful in the long run; certainly, it is difficult to see how the traditional advantages of the industrial district can be maintained if it continues. Subcontractors no longer have good reason to trust final firms which have the power to squeeze their profits at will. They are expected to provide flexibility without receiving any guarantees in return, becoming what Klaus Semlinger describes as “flexibility reservoirs.” (Semlinger 1993). This may, over the longer run lead to distrust, and persistently inefficient equilibria of the sort that have characterized final firm - subcontractor relations in sectors such as the European car industry (McMillan 1995). It may be possible to solve this problem through reputational means, and through creating an appropriate “culture” within these quasi-hierarchical structures (Miller 1992). One may note, however, that it is far more difficult to mitigate problems of distrust within hierarchy, where there are very substantial asymmetries of power between actors, than it is in situations where such asymmetries are less marked or non-existent.

Conclusions

In this paper, I have sought to make the case for a simple account of the relationship between trust (under the encapsulated interest account), distrust, and power. I have suggested that asymmetries of power, up to a certain level, are by no means incompatible with trust. Even when trust and its outcomes are asymmetric, trust may still be possible. Nonetheless, there comes a point where asymmetries are such that it is impossible for the more powerful actor to give credible commitments to the weaker. At this point, disparities of power prevent trust from arising, and make distrust the likely outcome. Where substantial asymmetries of power co-exist with uncertainty, it may be difficult for actors to be sure which side of this dividing line they are on.

This relationship between trust, distrust and power, may be shown to have implications for cooperation in the real world. In particular, it helps explain behavior in subcontracting relations between firms. If final firms wish to create the conditions for cooperation with their subcontractors, they are well advised to constrain their power in some way, whether through credible commitments, subjection to outside agencies, or other appropriate technologies. Failing this, they may find themselves in an inefficient equilibrium, where subcontractors rationally refuse to be trustworthy because they perceive that the more powerful party may simply take advantage of their good faith without reciprocation. Indeed, this last may be the default condition; it may take conscious effort on the part of final firms (as in Rhône-Alps), or the existence of external reputational mechanisms (as in Japan) to avoid it. Indeed, in many cases, final firms may prefer to pursue the profits possible through exploiting their power to the difficult and complex task of nurturing cooperation.[17]

Thus, while Becker and other critics of the encapsulated interest account of trust are surely wrong when they argue that trust reduces under this account to power, the encapsulated interest account may indeed incorporate power and its consequences. Indeed, precisely because it can provide a plausible account of the relationship between trust and power that helps explain the behavior of actors in the real world, it has an important advantage over those other accounts which have difficulty in so doing.

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1. This paper had its beginnings in a conference in the Russell Sage Foundation series on trust, jointly hosted by the Max-Planck Project Group on the Law of Common Goods in Bonn, and the Max-Planck Institute on the Study of Societies in Köln in December, 2000. I am grateful to Russell Hardin for having seen the germ of a paper in my arguments, and for having encouraged me to write it. I am also grateful to the other participants in the conference, especially Margaret Levi, Fritz Scharpf and Marco Verweij for their comments in discussion, and to Jack Knight, for later conversations on the topic. Indeed, this paper should be read in conjunction with a paper co-written by the author and Knight, which discusses the relationship between disparities of power, institutional change, and trust between actors.

2. See Hardin (forthcoming). "That we might not trust those who have power over us, especially when they have little reason to care for us individually, is no surprise. I depend very heavily on your favor while you depend not at all on mine. You can therefore do me substantial harm while I can do you little or none. The mutual trust that depends on reciprocal relations cannot easily develop in such unequal, non-reciprocal contexts."

3. I do not engage in an extended discussion of the encapsulated interest account here, only mentioning those points which are necessary to my argument. More extended descriptions of the encapsulated interest account can be found in Hardin (forthcoming) and Levi (1998).

4. I note that many authors disagree with this claim; specifically, there is dispute as to whether one can describe more general social relationships, such as citizens' relationship with their government, in terms of trust. I wish to bracket this set of issues. In this paper, I follow Hardin's definition, which emphasizes the relational aspects of trust. I note that some parts of my argument depend on such a definition; to the extent that one makes use of other concepts of trust, the force of my arguments will be vitiated.

5. This point is made in Hardin (forthcoming).

6. This argument adapts Knight's discussion of the distributional aspects of power (Knight 1992).

7. This point is the crux of Ken MacLeod's science fiction novel, *The Cassini Division* (MacLeod 1998). MacLeod, who has some acquaintance with game theory, asks whether it is possible for actors who are potentially immensely powerful, and are unconstrained by the "shadow of the future" to make binding commitments. His heroine reasons (correctly as it turns out) that they cannot.

8. As, in North and Weingast's example, when the Stuarts demanded loans under threat.

9. These situations are not incompatible, and may reinforce each other.
10. Note that this suggests how one may account for the effects of institutions and organizational forms on trust, in a way that does not reduce trust to mere institution-induced expectations. Insofar as institutions and organizational forms provide a technology which allows actors credibly to limit their future ability to use power in a manner that is inimical to trust, they may make trust between actors possible, without dictating the precise form that it

takes. Even where they do not produce trust, they may at least alleviate distrust. See further, Levi, Moe and Buckley (this volume).

11. Future collaborative work with Jack Knight will explore the relationship between institutions and trust in greater detail. For a useful critique of over-deterministic accounts of economic cooperation, see Lorenz (1999).

12. Note the limits of my ambitions here. I do not offer an explanation of why different outcomes may be reached in different settings; instead I wish simply to show that actors in each setting face a broadly similar dilemma.

13. See for example Holmström (1998), Sako (1991), Sako and Helper (1995). The literature on this subject is voluminous.

14. While Dore notes the presence of reputational mechanisms, his explanation clearly privileges social norms as an explanation, and in particular what he describes as "benevolence." While he is very likely right, most of the evidence that he advances is also compatible with a "narrow" rational choice explanation, albeit a more sophisticated one than the neo-classical market framework provides.

15. The following explanation builds on Lorenz's own explanation of business actors' reasoning, recomposing his arguments, as best as I understand them within the theoretical framework used in this chapter.

16. I here summarize findings that are laid out in much greater detail in Farrell and Knight (forthcoming) and Farrell (2001).

17. Susan Helper (1993) discusses the respective merits and problems of "exit" and "voice" strategies on the part of final firms. These closely parallel the strategies of pursuing power, or creating the conditions of cooperation, that I discuss here.