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The Emergence of Exchange Structures Revisited: Information Sharing, Trust and Endogenous Inequality

It has been shown that trust problems in economic exchange give rise to dyadic commitments -- i.e., long-term exchange relationships between specific trading parties. Returning to partners who showed to be reliable in the past allows actors to mitigate the risk of being taken advantage of, and such partner choice also provides incentives for honest behaviour. We revisit the question of how trust problems affect exchange structures. Arguably, institutionalized reputations systems are a key source of trust in modern economies. Reputations systems enable actors to learn from the experiences of others and thereby provide a basis for trust and trustworthiness that can substitute for the safety and incentives for honesty in dyadic long-term relations. Do trust problems no longer shape exchange structures in the presence of technologically facilitated large-scale reputation systems? We argue that trust problems still have far-reaching implications for market structures, but that the key feature they bring about is no longer dyadic commitments. We show in a game-theoretic model and in a laboratory experiment that in the presence of reputation systems, trust problems instead lead to the emergence of high market concentration, with all buyers frequenting one or a few sellers and excluding many others. The few sellers who are lucky to serve the whole market additionally earn a sizeable premium for their good reputation.