The Creation of Trust - The Interplay of Rationality, Institutions and Exchange

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Abstract

Relationships based on notions of trust represent a central aspect of the communitarian model of industrial districts. Examination of trust has generated a substantial literature; nevertheless, there have been relatively few studies that have empirically considered the sources of trust that operate in local ties and connections.

The paper aims to redress this imbalance by investigating relationships in the Arve Valley industrial district near Geneva. It considers sources of trust by engaging the theoretical framework of Möllering’s (2006a) model of trust which is predicated on the concepts of reason, routine and reflexivity. In conjunction with this, the field research employs in-depth semi-directive interviews with small firm managers in the Arve industrial district. The paper’s findings contribute to trust and industrial district literature by examining the complex interplay between the three antecedents of reason, routine and reflexivity in the creation of local trust in the industrial district setting. In essence, the paper proposes that the availability of information about potential partners and the existence of strong interdependencies inform trust decisions based on evaluation and calculation more than local norms and institutions.

Keywords: Reason, Institutions, Trust, Industrial Districts, Arve Valley.
Introduction.

In spite of considerable advances in understanding trust in a wide variety of situations and contexts over the past twenty years, a number of areas continue to be under-researched. One of these is the creation and development of trust in industrial districts.

Trust, defined as;

‘the willingness of a party to be vulnerable to the actions of another party based on the expectation that the other will perform a particular action important to the trustor, irrespective of the ability to monitor and control that other party’ (Mayer, Davis, Schoorman, 1995, 712),

is considered to be axiomatic to the communitarian model of industrial districts (Harrison, 1992, Dei Ottati, 2002, Lorenzen, 2002, Staber 2007).

The overwhelming focus of the work carried out in this regard has concentrated on the examination of the positive effects of trust on inter-firm relationships. This research rests in stark contrast to the possibility of conducting empirical investigations into the factors which might contribute to the formation of trust (Staber, 2007). As the following review of industrial district literature on trust will demonstrate, authors are divided between three possible sources of trust. One recurrent theme concerns information availability. High levels of information from overlapping business and social networks, combined with expert observation and mutual interdependency, reduces information asymmetries and permits agents to calculate the likelihood that trust will be honoured (Lorenzen, 1998, Oba and Semercioz, 2005, de Propris, 2001). A second, sociological stream is based on the idea that strong socialisation processes create and reinforce local institutions. Thanks to a long history of trust and cooperation in a tightly bonded group, trust becomes ‘normal’ or the ‘default setting’ for intra-district transactions (Boschma and Lambooy, 2002, Bellandi, 2002). As such trust becomes a ‘habit’ or a ‘routine’, (Möllering, 2006a). To what extent these routines and habits become automatic and unthinking is a matter of debate and difficult to investigate (Hogdson, 2006, Bachmann, 2011). Finally, most authors would concur with Harrison (1992) that frequent face-to-face meetings in a variety of settings lead to agents learning to trust one another (or not). The confusion evidenced in district literature stems from the fact that trust is a multi-dimensional phenomenon which builds on multiple sources.
We propose to tease out these multiple strands so as to clarify and highlight each source’s contribution to the creation of trust. But, because each source is closely intertwined with the others, we shall then proceed to examine their interaction and interplay. Such data can assist in addressing the question of the creation of trust and its antecedents.

This paper aims to address the above-identified gaps in the literature by examining the creation of trust in a dynamic industrial district in the south-east of France: the Arve Valley bar-turning or lathe working district situated between Geneva and Chamonix-Mont Blanc.

We shall attempt to analyse the creation of trust between small companies in intra-district exchanges and the inter-play between three different foundations of trust which can be outlined as reason (calculation), routine (institutional) and reflexion (process) as postulated by Möllering (2006a) (itself based on Lane’s 1998 typology). A more complete discussion on the strengths and weaknesses of different trust models would make for an interesting paper in itself, but space restrictions do not allow for this here. The difficulties come from the necessity (or impossibility?) of creating a model which could include all the reasons that we would trust in a given situation (Möllering, 2006a). This poses the problem of creating a model which, in a sense, depicts and explains an agent’s worldview, which is clearly an impossible task. Möllering’s (and Lane’s) approach has the major advantage of being ‘holistic’ and defining and analyzing both antecedents and literatures of trust. It does not impose any particular a priori vision of what a particular agent’s worldview might be.

The paper is structured as follows: firstly, it examines trust as portrayed in the industrial district literature by applying Möllering’s (2006a) typology. This exercise surfaces a number of inherent difficulties related to the fact that many authors mix and match their approaches causing frequent contradictions and confusion. This is followed by a discussion of the research methodology while the final section will present and discuss the implications of field data based on in-depth interviews with small company manager/owners.

**Literature Review: Trust in the Context of Industrial Districts**

As alluded to above, while trust has been addressed and discussed in-depth in a range of situations and contexts, the origins of trust in an industrial district setting has received relatively minor attention (Staber, 2007). The present argument works to address this issue by employing a range of sources and engages Möllering’s (2006) widely cited framework on
trust which is predicated on the concepts of reason, routine and reflexivity. The paper’s argument is kindred in spirit to Nooteboom’s (2002) argument in that trust builds through reflexive and intertwined processes based on reason and routine, however the present argument develops from Nooteboom’s overall position and posits that process based trust has difficulty accounting for, on its own, why someone would take the first step to trust. Among other issues, the argument below seeks to address this and considers each of these dimensions in turn. In doing so, it is important to say that the paper acknowledges that these elements operate in a dynamic and symbiotic manner rather than to suggest that they operate completely independently of one another. However, for the purposes of analysis it will be useful to consider them gradually and in a phased manner.

**Trust as Reason in Industrial Districts**

The rational choice model (also referred to as reason or calculative-based) describes trust as a function of perceived trustworthiness (Mayer et al., 1995). Those individuals who decide to trust, or *trustors*, will look for signs and information which will help them to calculate the probability that their trust will be honoured (Coleman, 1990). While people undoubtedly do *evaluate* the trustworthiness of possible partners (Dietz, 2011) and the corresponding probability of betrayal, the approach has limitations in three important ways. Firstly, how much unambivalent information is available to each agent? People who desire to be trusted may send out signals intended to be interpreted as signs of trustworthiness. Secondly, it is important to consider the extent to which a rationally-bounded agent might be able to calculate all possible future payoffs from an existing exchange situation. In particular, it may be difficult for agents to calculate (all) the utility function(s) of exchange partners. The third weakness of the rational choice model is its reluctance to integrate institutional constraints beyond the calculation of a partner’s likelihood of breaking rules and norms. That is to say, institutions are taken to be external constraints. The approach assumes agents share expectations, norms and values which condition future desired outcomes; whereas norms, values and rules are simultaneously created and questioned by agents through social intercourse (Murphy, 2006). Institutions may be placed on a continua between those which are debated and decided by actors, the road code for example, and those which, like one’s mother tongue, while not innate, are acquired socially and interiorised to such an extent that they are no longer questioned (Hodgson, 2006). Bachmann (2011) underlines the difficulty of examining the roles of the interiorised norms in trust studies.
Moreover, several authors reject a reason-based approach to trust creation in industrial districts and not necessarily with reference to the arguments developed in the trust literature as discussed above. Dwivendi, Varman and Saxena (2003) indicate this bias when they discard reason based or calculative trust because:

“deterrence and calculus based trust, with their narrow motivational aspects, do not match the description of cooperative inter-firm relations in the industrial district literature” (p.96).

This remark may seem to exhibit aspects of naivety in that it implies that industrial district firms only cooperate and that there is a complete absence of rivalry and competition among geographically proximate firms. Certainly, the industrial district literature underlines the unique mixture of co-operation and competition found in industrial districts. Cooperation exists, but firms simultaneously manifest cooperative and competitive strategies.

The (ideological?) bias against reason as a basis for trust may stem from the fact that economists examining industrial districts have often excluded trust from their analysis, or, on the other hand, it may be the case that other social scientists (for example, sociologists, geographers) have analysed industrial districts primarily through sociological and institutional lenses. For instance, Dei Ottati (2002) does not provide arguments for this rejection apart from preferring an institutional or routine basis (similar values and common rules of behaviour).

Routines can be created over time when actors recognise their utility in certain situations (trusting local suppliers in our case). In highly socialised contexts such as industrial districts, strategies (routines) which have proved successful in the past are handed down through generations of people working in the same industry as the ‘way we do things here’ because,

‘experiences of firms within the cluster would promote the continued evolution of similar mental models of strategists and managers’ (Pouder and St John, 1999, 1200).

Managers may imitate what seems to be a superior strategy (and trusting partners seems a superior strategy: the success of district firms attests to this), not because the routine is superior but because imitation and adoption may be less costly in terms of speed and cognition when compared to efforts that individual learning demands of them (Staber, 2009).

District scholars have tended to see the result (norms of forebearance for example, Bell, Tracey and Heide, 2009) rather than delve into the creation and replication of the institution.
Overall, the rejection of reason or calculative-based approaches as a basis for trust is common among industrial district scholars. For example, Humphrey and Schmitz (1998), eliminate reason based trust on the grounds of game theory (the backward induction argument), however, at the same time, they recognise interdependence between highly specialised district firms as a central element of district relationships. From this awareness of interdependence is born the notion of ‘encapsulated trust’ (Hardin, 1992), which is a form of calculative trust;

‘...firms relate to each other on the basis of mutual complementarity and above all interdependence. The latter, in particular provides a crucial condition for trust to root.’
(De Propris, 2001: 746)

Another central pillar of the industrial district model is what might be termed the ‘transparency’ hypothesis. Districts are considered to be places where information flows freely and rapidly thanks to overlapping business and social networks and expert observation. Actors have large amounts of information concerning possible exchange partners. Their history, reputation, and technical competence for example, are assumed to be known throughout the ‘community market’ that comprises the district (Maskell and Lorenzen, 2004, Maskell, 2001, Lorenzen, 1998, 2002). Although complete information is impossible, actors in districts have, in theory, enough information to calculate trust with intra-district partners.

Maskell and Lorenzen (2004), have no qualms relying on actors’ capacity to calculate payoffs thanks to abundant information in ‘transparent’ local markets. They do not pretend that districts are pure and perfect markets, but suggest that actors possess more information than ‘average’ and this facilitates calculating trust. Complete and perfect information however would negate the need for trust as it would eliminate the very uncertainty which is central to the concept.

In summary, abundant information facilitating calculation is a common theme in many approaches to trust in industrial districts, but echoing earlier arguments of the complexity of social life and an agent’s cognitive limits, Dupuy and Torre (2004: 4), maintain that, by definition, with incomplete and partial information ‘an actor must make a subjective estimation’ to trust. No matter how incomplete, partial or approximative the information available, Dietz (2011) maintains that reason is the first universal step on the path to trust decisions. The word subjective now brings us to regard how scholars in district literature have analysed trust which draws on institutions, both formal and informal.
Routine or Institutional-Based Trust in Industrial Districts

Institutions are the ‘structural arrangements represented by rules of behaviour to which individual and collective behaviour is orientated’ (Bachmann and Inkpen, 2011: 285). They include formal, explicit rules of behaviour such as laws and context specific informal rules which acquire legitimacy over time when groups accept and integrate them into their behaviour (Bachmann and Inkpen, 2011). There is however a paradox to take into account; if rules, norms, routines and institutions in general are so interiorised that the actors follow them blindly, then there is no need to call upon trust, other than to call it blind trust because the interiorised institution would eliminate the doubt and uncertainty so central to trust.

Reflections upon the institutional basis for trust must go beyond considering institutions as external constraints and whether trustors are capable or not of calculating the likelihood of a partner respecting these rules. Such an approach, common in much management trust literature, is too narrow and reduces trust research to questions of individual cognition or interpersonal social-psychological processes (see, for example, Möllering, 2006b, Bachmann and Inkpen 2011 on this issue). Many actors may not be entirely aware of the influence of institutions on their behaviour because these rules that structure social interactions may ‘never be purely or fully matters of conscious deliberation’ as they may be deeply rooted in tradition or habit, (Hodgson, 2006; 4). An institutional approach obliges us to take into account the context of trust decisions and to examine the concept of ‘embedded agency where trustors and trustees, as actors, interpret the social context in which they are embedded’ in conjunction with the ‘normalness’ of the actor’s environment and their familiarity with it leading to a ‘natural attitude’ (Möllering, 2006b:356-358). In other words, actors consider trust as the ‘normal’ ‘way we do things here’. Intra-district trust in much of the literature thus becomes a default position; a behaviour positively reinforced by the existence of many successful examples in the actor’s immediate environment (Staber, 2007). This constitutes a form, in fact, of mimetic isomorphism whereby emulation of other firms becomes a mechanism for survival (DiMaggio and Powell, 1983).

Möllering’s (2006a) framework divides issues relating to institutions into three subsections; rules, roles and routines, each of which contribute to creating a context where trust is no longer questioned but becomes part of an agent’s normative behaviour. We have already mentioned the idea of rules above: they have the property of co-ordinating expectations and therefore reducing risk (Lane, 1998) and ‘Trust means... interacting with others on the basis
that everyone knows and accepts the basic rules for that interaction’ (Möllering, 2006a: 58). It is vital that: a) an agent must know the rules of the game, and, b) believe that the other player knows them and, c) believes that the other player will respect the rules because breaking them involves sanctions (Garfinkel, 1963). Coleman (1990) notes that networks which are too large will dilute the force of the rules and reduce the likelihood of being seen and punished.

‘Roles’ refers to ‘types of actors in a context where action is typified and available as common knowledge to a collectivity of actors’ (Möllering, 2006a: 68). Roles allow individuals to participate and interact in a social world. For Möllering, roles carry ‘the taken for granted expectations on which trust can be based’ (ibid; 68). Roles become part of a ‘natural or normal world’ which contributes to trust between actors who recognize how each person will behave according to their particular role. In this way, agents create a world in common with social partners and rely on this fiction to provide stability and meaning to exchanges.

Alternatively, routines are defined as regularly performed programmes of action or procedures which may or may not be supported by rules and roles. They contribute to trust by providing cues to actors as to what is ‘normal’ or ‘everyday’ and therefore provide sequences of likely of actions and predictable outcomes which help actors minimize their vulnerability. In recognising this, we must not ‘over socialise’ the actor and insist that the decision to trust cannot exclude agency. Thus, Möllering talks of ‘embedded agency’. This concept is particularly relevant to industrial districts because the very intense in-group socialisation processes in action create and reinforce behavioural models (Mistri, 2003).

Routine-based trust in industrial districts is implicitly acknowledged by many authors for whom trust is simply there. It is part of the texture and history of the region, as described by Putnam (1993), where a long history of horizontal bonds between people in north-eastern and central Italy, dating back to the early medieval period, lead to collaboration amongst people and firms, of which Italian industrial districts are a manifestation. A number of authors propose a ‘local culture’ of trust or that trust is a ‘local capacity’ which takes its source from shared histories and experiences of decision makers (Boschma and Lambooy, 2002, Eraydin and Armatli-Koroglu, 2005, Gordon and McCann, 2000). Amin (1999: 393), talks of ‘broader communitarian ideology of co-operation and consensus’ as the basis for trust. Trust in this stream is theorised as being part of the ‘deep structure’ of the district but little empirical evidence is provided in support.
While institutions exhibit deep rooted, socially reproduced and validated habits and assumptions (Hodgson, 2006), it would be erroneous to over-socialise actors in industrial districts and thus render them devoid of the agency which is central to trust decisions. When looking at questions of reason versus institutional based trust in districts, we should bear in mind the inherent duality of agents creating, modifying and questioning the institutions inside which they are evaluating trustworthiness and the probability of aligned future expectations (Murphy, 2006).

Industrial districts are highly socialised, spontaneous productive systems; agents act within the constraints of local institutions, but many authors in district literature assume an automatic causal link between (generally unspecified) local institutions and trust - a link which is overly generalised and empirically untested.

**Reflexivity or Process-Based Trust in Industrial Districts**

The third foundation for trust, ‘reflexivity’, or process-based trust, is the common sense notion that trust is built up slowly over time through repeated interactions where agents learn about each other’s expectations, values and construct their world in common; i.e. agents verify that the other player plays by the rules. The reflexive creation of trust may lead to strong ties but being slow and time consuming may not be economically efficient or even feasible (Bachmann and Inkpen, 2001).

Many authors implicitly accord importance to the reflexive construction of trust between district actors because local exchanges are assumed to be more frequent, intense and long-lasting and district actors share the same values norms and ‘social codebooks’ which facilitate communication. For example, Maskell and Malmberg (1999) seem to take a process-based approach to trust building; ‘Firms build trust-based relationships by piecemeal committing themselves economically and socially’, (p18). They also suggest that trust becomes a habit (therefore an institution?) as ‘(the) default (setting) is trust if nothing is known of the firm’ (p18). It is difficult to follow the logic here: trust is built up over time through mutual investments and adjustments except when dealing with unknown firms when trust is the default setting? Trust eventually becomes a shared ‘routine’ amongst actors (p18), therefore an institution? Process based trust depends on communication and interactions between actors; it is assumed that more interactions lead to more trust. Rare are the authors who question such assumptions, (Staber, 1998, 2007).
Murphy (2006) underlines the reflexive nature of trust creation, considering it to be a dynamic social process which calls upon actors’ ‘bounded rationality’ and but also ‘the attitudes, feelings, props and visual clues which are mobilized in the process of constructing trust’, (p435). In bounded rationality, social interactions are shaped by interpretive frameworks or situational definitions. Trust building processes are ‘communicatively driven’ (p.440), while role playing enables individuals to ‘objectivise themselves’, therefore permitting social actors to generate meanings about what trust is and lead to a stabilised understanding of its implications. These shared meanings and expectations of roles to be played lead to distinct economic practices and outcomes as is the case in industrial districts. An individual’s perception of trustworthiness (of the other) and the expected behaviour in a given situation will be shaped, for Murphy, ‘by the degree to which inter-subjectivity is achieved in the communication process’, (p438).

Frequent face to face meetings and repeated exchanges allow actors to exchange information, align expectations and verify adherence to local norms and therefore build trust by an interactive learning process (Harrison, 1992). However neither Paniccia (1998) nor Staber (2007) accept this proposition; both pointing out that some clusters or districts seem to generate antagonistic or distrustful relationships.

**Methodology**

The Arve Valley is a metal working, bar-turning or screw-cutting district. Bar-turning is perhaps the best translation for the French word *décolletage*. Bar-turners are lathe operators who traditionally cut screws and precision parts for the Swiss watch industry (Geneva is situated 50km away). The heart of the district is comprised of 288 bar-turning firms (industrial classification code NAF 25.62A), centred around the town of Cluses. The industry is supported by a variety of specialist supplier firms and institutions, such as a research centre, raw material and machine suppliers, and surface and heat treatment firms. Approximately 90% of the district bar-turning firms are small or very small companies with fewer than 50 employees.

We interviewed 19 small firm owner-managers of bar-turning firms all based in Cluses or adjacent villages. We selected small bar-turning firms from the on-line trade directory found on the Tecnic Vallée website (the French label for this district). Our sample corresponds to the small firm owners who accepted to spend approximately one hour in a semi-directive
interview. The respondents form a coherent group. Only three of the 19 companies were run by what we could call ‘outsiders’; people who had not been raised and educated in the valley. In the sample, 14 of the 19 companies were family firms, some in their 5th generation: 6 of the 19 were run with members of the close family, either siblings or, in one case, cousins.

We chose to use a qualitative methodology because in order to unpack such a complex, nuanced concept as trust it is necessary to developed contextualized accounts (Kramer, 2006, Nootboom 2006). Trust research must confront several methodological problems. If we define trust as a psychological state, the willingness to accept vulnerability, (Rousseau, Sitkin, Burt, and Camerer, 1998), which leads to a decision to make oneself vulnerable, it will be necessary to observe manifestations of trust (Li, 2012). Respondents may also take trust for granted and therefore have difficulty in describing an attitude which is ‘normal’ or part of the daily fabric of their business lives. The question of trust may only arise when it is ‘put to the test’, that is, when unforeseen problems or misunderstandings arise (Möllering, 2006a: 188). ‘Suppliers will only find out how trustworthy the customer is when short-term interests favour betrayal’ (Humphrey and Schmitz, 1998: 50). If asked directly about why they trust a particular partner, responses could be rationalised ex-poste in order to justify decisions.

Asking direct questions about why a respondent trusts (or trusted) in a specific situation runs the methodological risk of having respondents rationalise and justify previous decisions which may have been made through interiorised norms or conventions (Luhmann, 1979 in Möllering 2001). The salient point of norms and conventions is that the agent may not be fully aware of their influence on their behaviour (Hodgson, 2006). Respondents looking for ‘good reasons’ to explain trusting behaviour may fall back on seemingly rational responses such as, ‘they are technically competent’ for example, where the question of competency and trustworthiness was proved ex poste and may not have entered into the original decision making process.

In order to avoid these methodological pitfalls and develop a coherent context of trust in the district, we avoided mentioning the word ‘trust’ in our interviews and focused on problems that had arisen between bar-turners, their colleagues and suppliers and discussed where the problems came from and how they were resolved. Figure 1 (below) demonstrates the different exchange relationships discussed.
Figure 1: Exchange relationships discussed during interviews.

We are drawn to investigating the creation of trust in industrial districts in the following terms and shall attempt to answer Harrison’s (1992) question: ‘… from where does this trust emanate? What reproduces it?’ To which we add the following research questions:

To what extent do industrial district actors generate trust in local exchanges?

Which of the three antecedents of reason, routine or reflexion, if any, dominates trust creation?

And finally, in what ways do the three antecedents intertwine and combine to create trusting relations between firms in industrial districts?

Results and Discussion

Our empirical investigation of the Arve Valley industrial district confirms the presence of a trusting co-operative environment between small firms conform to district literature. Lack of space prevents us from detailing every element but the following examples are indicative; managers rarely used contracts for local transactions, tools were lent between firms, raw material was ordered over the telephone, firms grouped together to produce for upstream clients labelling the parts according to whichever firm had the necessary quality certifications. Intra-district relationships give us ample opportunity to analyse trust and its three antecedents of reason, routines and reflexion. Specialised firms are highly interdependent, (‘We need you and you need us. It’s a win-win situation’ said Manager 12 talking of his local suppliers). Their owners share similar world views and are embedded in an all-encompassing social environment and they interact frequently over many years.
Our research reveals the strength of local ties. Managers seemed prepared to go to some lengths in order to maintain local ties with suppliers and other bar-turners. Managers talk of a ‘diplomatic craft’ and not ‘wanting a conflict’ (Manager 13). ‘If he (a local supplier) makes a mistake, we’ll try to make the relationship continue’, Manager 7. This indulgent and compromising behaviour is a rational strategy because it protects their company’s competitive advantages. Central concepts and their links to existing trust or district literature are summarized in figure 2 above. Concepts such as ilunga, indulgence and gift-giving, new to district literature will be discussed in length below.

**Reason**

The first ambiguity in the literature we are able to address is the question of calculation or reason as one of the foundations of trust in industrial districts. As mentioned above, authors taking a predominately institutional approach seem to follow Lane’s (1998) criticism of reason as an inadequate basis for trust and therefore reject it out of hand. This rejection implies a negation of agency which would have as effect the repudiation of trust (no decision to trust by over-socialised actors). While the possible validity of a reason based approach to trust creation may serve as an *a priori* assumption for transactions and behaviour, reason may be insufficient as a *sole basis* for trust. We contend that agents do *evaluate* the likelihood of
their trust being honoured because of two fundamental aspects of district dynamics; transparency (i.e. the availability of salient information) and interdependency.

**Transparency**

Valley firms benefit from high levels of information concerning prospective partners (Dupuy and Torre, 2004). ‘There’s a type of scrutiny, always knowing what the other guy is up to’ (Manager 6). Information circulates in social and business networks facilitating the calculation of the likelihood of opportunistic behaviour. In a district where family firms are common (14 out of 19 of our sample) information circulates in family and social circles:

‘Jean-Claude (a bar-turner) is the father of a friend’s wife’ (Manager 3), or ‘He’s a cousin…he married the daughter of an aunt who is our cousin’ (Manager 12).

Transparency also originates from the fact that over 90% of the firms in the district do not exceed 50 employees; as such they have very similar cost structures. This situation leads to rapid agreement about sub-contracting prices between valley bars turners; ‘excessive prices are easy to see’ (Manager 17) and ‘we know the right price’ (Manager 15).

From an informational and calculative point of view, managers possess sufficient knowledge to be able to calculate who to trust. However, although several respondents affirmed that ‘everyone knows everything in the valley’, and ‘there are no secrets in the valley’, it was interesting to note that some managers had to resort to using local trade directories to find new sub-contracting firms with specific machines and skills. There is, it seems, insufficient information and enough uncertainty in the district to make calculating partners’ future behaviour difficult.

The combination of district transparency, that is to say information flows and observation and small networks inhibits opportunistic behaviour (Maskell and Lorenzen, 2004, Coleman, 1990), or as Manager 16 said, regarding sub-contracting prices in the valley: ‘A price too high would be seen straight away’. Manager 7 concurs; ‘When someone says that part there costs 3 euros, I know if the guy’s lying or not’. Whether ‘everything is known’ in the district is true or not, managers seem to take transparency as a given in their relationships, and act as if their actions will be known by all in order to protect their reputations (thus adhering to Garfinkel’s 3 rules described above). One manager mentioned that he avoided putting himself in a position where he could be accused of poaching clients by not going personally to surface
treatment or transports firms (where products are laid out with clients’ names and addresses in full view).

**Interdependency**

A second pillar of reason at work in constructing trust is the case of interdependencies from mutual subcontracting which leads to ‘encapsulated trust’ (Hardin, 1992). Work is contracted out to other bar-turners for reasons of both scope and scale. It is not infrequent for firms to inverse their roles over time according to machine specialisation and availability. ‘I have a lot of clients who are occasionally my suppliers, and there we are on equal footing because we need each other’, (Manager 12).

When choosing a new sub-contractor Manager 11 rapidly accepted to work with a firm recently created by two younger bar-turners even though she ‘didn’t know them that well’. Her decision to trust was made easier because she knew that the start-up needed work and needed to develop its network, relationships and reputation in the valley. The start-up has an obvious interest in showing itself to be a competent sub-contractor and becoming a worthy, long-term partner. The sub-contracting firm knows that the start-up needs business and seemed comfortable in trusting the new company because of the encapsulated nature of the relationship (based on their mutual objectives). Manager 12 talked of a ‘win-win’ situation with suppliers, while Manager 2 considered suppliers to be ‘partners’, Manager 6 explicitly mentioned that bar-turners and suppliers needed each other.

The stakes involved in this mutual sub-contracting clearly demonstrate two aspects of reason based (or calculative) trust, namely encapsulated trust and the shadow of the future (Axelrod, 1984). Bar-turners do not possess their own products or brands. They depend uniquely on upstream clients in the value chain and other bar-turners. Other bar-turners may provide work in the future and, at the same time, provide the possibility of increasing one’s production capacity and/or one’s range of products. In both cases out-sourcing work leads to increased customer satisfaction from increased flexibility. Sub-contracting between bar-turners is therefore a critical element of a small firm’s competitiveness. It is therefore a perfectly reasonable and calculated trust decision to give and honour trust in this situation.

Relationships between local bar-turners are generally trustworthy because reputation effects in small networks, encapsulated trust and the shadow of the future all contribute to the logical appraisal by bar-turners that trust will be honoured. It reinforces horizontal ties above and
beyond, say, adhesion to a local trade organisation. These dyads among the central firms of the district form the template for other relationships in the valley.

**Routine and Institutions**

Bar-turners seem to follow logical strategies of maintaining their reputations through fear of sanctions (Manager 7 maintains that he avoids putting himself in the position where he could be accused of poaching clients), or evaluating the motivations of a partner to ensure that mutual interests coincide and subscribe to the notion that honourable behaviour today will pay economic dividends in the future. Yet we have found many examples of behaviour where bar-turners seem to adhere *blindly* to local norms, act in altruistic ways and seemingly put the communities interests before their own. Behaviours which, on the surface, seem to contradict self-interested utility maximising behaviour. We examine these issues under the themes of: community spirit, norms and values and fairness and honesty. But firstly some remarks on institutions.

**Implicit and Explicit Institutions**

The examples detailed below illustrate locally developed and agreed upon institutions. As such, given the network structure of intra-district relationships and the relatively small number of participants, it is a perfectly rational strategy to be seen to obey these rules and thus inspire trust. However, things become more complicated when trust decisions are structured by interiorised norms which may not be recognised explicitly by the actors themselves (Hogdson, 2006) and difficult to reveal in the field (Bachmann, 2011). During our interviews we frequently found ourselves playing ‘devil’s advocate’ suggesting that local firms may take short-cuts and display opportunistic behaviour. In general our suggestions were met with blank and uncomprehending stares by our interviewees. For example, when we suggested that a heat treatment firm may not heat a piece to the required temperature (to harden the steel), Manager 3 replied that they wouldn’t do that because the supplier issues quality certificates. This is a common enough occurrence except that the certificate wasn’t issued by a third party but *by the suppliers themselves*. Manager 3 couldn’t see why the supplier would cheat. Manager 8 was so surprised to be questioned along these lines (local suppliers and ‘partners’ may not be trustworthy), she replied ‘why would they cheat?’
Community Spirit

According to Luhmann’s (1984) theory of social systems (analysed and extended in Lane and Bachmann, 1996) a minimal social system is established once a boundary between an ‘inside’ and an ‘outside’ is established. The ‘outside’ is seen as unlimitedly complex, while the inside is seen to turn around a selection of some specific system properties. Hollis’ (1998) desire to see trust built on a logic of ‘us’ rather than a logic of ‘me’ finds its empirical manifestation in functioning industrial districts as described by the ‘Italian’ school (Becattini, 1992, Dei Ottati, 2002 Alberti, 2006). Becattini (1992) spoke of a ‘sense of belonging’ that defined the district.

We found that bar-turners were conscious of belonging to the same social group which has clear, common goals. One bar-turner (Manager 18), not able to manufacture a piece, made sure that the order stayed in the district. Examining interview transcripts reveals an interesting aspect of district managers’ world view. Very few respondents mentioned the word competitor during an interview, except to draw attention to competitors in Romania and China. Apparently there is competition between different industrial district firms (accepted as being a normal part of the game), but no competitors within the district. While Porter’s (1990) cluster model posits local rivalry as a driving force for innovation, we found that bar-turners in the Arve valley did not believe they had direct competitors in the valley. Managers can avoid direct competition because high levels of information and multiple downstream markets allow entrepreneurs to find market niches where a start-up could avoid direct local and even national competition - the district accounts for approximately 60% of French production. Local competition exists but is tempered by niche strategies among local companies. This situation facilitates inter-firm cooperation.

‘Even with this recession, there is enough place for everybody’ (Manager 5).

Bar-turners exhibited a marked tendency to empathize with other small business managers in the district, considering that everyone had the same constraints and preoccupations. ‘My neighbour is a colleague not a competitor’ (Manager 14), or, ‘we all come from production side of the business’ (Manager 5). With local firms ‘we have the same mentality’ (Manager 6).

The most obvious examples of ‘us and them’ were linked to district and occupational identity (and therefore the right role to play). Bar-turners had very clear ideas about who they were; ‘sons of bar-turners’ for example, while outside clients such as the auto-industry were
described as ‘sharks’. There was a clear barrier between technicians (like the bar-turners) and non-technicians (professional purchasers from outside for example). Trust between local managers was reinforced by the fact that they were all extremely similar in terms of upbringing, training and experience and, in the same turn, expressed clear differences in relation to outsiders from beyond notional valley ‘boundaries’.

**Norms and Values**

Local norms created by the community contribute to group cohesion in that they permit agents to align expectations of permissible behaviour. Three local, explicit ‘rules of the game’ emerged from the research:

- Don’t steal a colleague’s client directly (i.e. by deliberately contacting the client and proposing a better price as opposed to ‘loyal’ competition, i.e. being contacted by a prospective client);
- Don’t poach other district firms’ skilled workforce;
- Finally, don’t reduce prices during an economic downturn.

It is worth remarking that the rule about not stealing a ‘colleague’s’ client was very clear and unambiguous. However, many managers noted that it was extremely difficult to know if the rule had been broken. How could a manager know that another had prospected a client or that the client had asked several valley firms to bid for work? When asked if they knew of firms who had broken this norm, managers replied yes, but refused (or were unable) to divulge names.

**Fairness and Honesty**

When bar-turners sub-contract out work to each other there seems to be little discussion about prices. The goal (when sub-contracting out to other valley firms) is ‘not to make money (by squeezing) suppliers’ (Manager 5). A ‘fair’ price was proposed. A price which included an ‘acceptable margin’ which allows the supplier firm (another bar-turner) to make money from the work. This norm of equity was based on information available in the industrial district. Information asymmetry about the sub-contractors costs was very low (same machines, similar techniques, similar firms, same rents), and the margin shared between the two firms was conditioned by the (outside) client’s acceptation of the sub-contracting firms price. Bar-turners accord each other, and agree rapidly on, a ‘fair’ price (i.e. one which includes a fair
the long-term advantages of co-operation outweigh short term gains from haggling over prices (and as mentioned above, they know each others’ cost structures). Imbalances in the exchange relationship will even out over time or the relationship will be terminated (Mauss, 1950: 1990, Blau, 1964).

However, if information asymmetries are very low between the two firms inside the industrial district, they are relatively high between the outside client and the focal bar-turner. The focal bar-turner appropriates added value from the client in the form of an acceptable margin and distributes this margin among their network partners in the district. A ‘fair price’ therefore is an institution that arises from intimate knowledge of cost structures and a ‘us and them’ mentality where cost structures (and sub-contracting practices) will be hidden from the outside client. The automobile industry’s relentless drive to unveil suppliers’ cost structures and squeeze margins wafer thin is one reason why bar-turners dislike them and consider them ‘disrespectful’ because they do not respect the local norm of a ‘fair’ price and a ‘living’ margin. The institution of a ‘fair price’ however, is not uniformly respected across the district. Certain wholesalers and bar-turners, conscious of cost-structures, will knowingly offer razor-thin margins to bar-turners for sub-contracting work in the hope that a firm, in need of business, will accept to work at prices which will only just cover costs.

When bar-turners are interrogated about the honesty of fellow industrial district managers they tend to rationalise their assumptions of honesty in a manner which illustrates the interplay between information flows and local institutions. Bar-turners explain the honesty manifest in the district by saying that their craft is essentially ‘transparent’ and ‘obvious’. A piece or component either fits or it does not. It is either the right size or it is not. In other words, they explain honesty not through any higher morality but rather through the impossibility of getting away with opportunistic behaviour.

**Reflexivity and Process-Based Trust**

District literature underlines how geographic proximity facilitates intense and frequent exchanges which diminish information asymmetries and create inter-personal bonds between similar agents. Managers seemed to feel that geographic proximity simply made life easier, for example when managing supplier relationships, ‘because these people are nearby we can react rapidly, go and see them to discuss technical problems and other things’ (Manager 2). Choosing a new sub-contractor (a bar-turner) was easier because ‘they’re not far from here’
even though ‘we don’t know them that well’ (Manager 11). Metal suppliers ‘are local, so we know we pay the (right) price’ (Manager 6).

**Indulgence and Ilunga**

Managers go out of their way to accommodate ‘mistakes’ and ‘misunderstandings’ from local suppliers. Possible bad faith or opportunism on the part of local suppliers was evoked only once. Surface treatment firms received a particularly indulgent treatment in terms of conflict management. They ‘don’t have highly qualified staff’, or they work in an activity that is like ‘cooking’ (Manager 7); i.e. following the same recipe won’t always give the same results. Of particular interest was the indulgence accorded to local exchange partners:

‘I tend to be indulgent, above all if he’s never given us a problem before. I’ll give him one chance, the second time I’ll ask myself questions, the third time it’s no longer possible to work with him’ (Manager 5).

This ‘3 strikes’ rule is similar to the concept of *ilunga*, from the Tshiluba language spoken in the south-east of the Democratic Republic of Congo, meaning "a person who is ready to forgive any abuse for the first time, to tolerate it a second time, but never a third time" (Conway, 2004). When discussing conflicts between bar-turners and local suppliers, opportunism was never invoked by the managers interviewed. Problems were perceived as originating from mistakes rather than from cheating, (similar to Uzzi’s 1997 observations in the New York garment district). The frequent examples of *ilunga* attest to managers’ desire to keep the relationship alive even when they suspected that something was not right.

More interesting still is the compromising when sharing the costs after the mistake has been admitted and the blame attributed. The sharing of the costs by the bar-turner who refuses to exploit his superior position is a type of *gift-giving* which creates and maintain social ties (Godbout, 1992, 2004; Mauss, 1950:1990). Gift-giving creates a feeling of obligation to reciprocate in the exchange. As a Guinean proverb puts it; the hand that receives is always under the hand that gives. The objective is to create the conditions for reciprocity which reinforce the social and moral strength of the commercial tie. Managers compromise and maintain long-term relationships with other partners because they wish to ensure their own competitive advantage. Their competitive advantage (and that of the industrial district)
depends partly on the competitive advantage of their suppliers (akin to Porter, 1990) and the strength of their network relationships. Adaptation to other local partners represents investments which must be maintained and are, as such, sunk costs (Maskell and Lorenzen 2004). Bar-turners compromise with local partners in order to profit from these previous investments. They go out of their way to maintain local ties by being indulgent (but not naïve), and compromising when problems arise because suppliers (almost exclusively local) represent important sources of competitiveness, flexibility and innovation.

**The Interplay of Three Antecedents: Reason, Routine, Reflexion.**

Trust creation depends on a combination of sources and antecedents. We have attempted to tease out the different strands of trust creation in industrial districts above in order to clarify and simplify a complex, subtle and multi-dimensional phenomenon. In the following section we shall examine how these different elements combine to produce trust.

![Diagram of Antecedents and Interactions](image-url)

**Figure 3:** Antecedents and interactions in trust creation in the context of industrial districts (after Möllering, 2006, 110).
Starting with the interplay between reason and reflexivity, we have discussed above examples of Arve valley managers calculating their trust decisions based on information available to them and their evaluation of their partners’ motivations to honour trust or not. These hypotheses of trustworthiness are then validated through frequent exchanges and risk reduction. There is however ambiguity in this situation because although some managers started relationships with small trial orders (conform to Lorenz’s 1998 study of inter-firm subcontracting), more than one manager began new sub-contracting relationships with ‘normal’ orders, suggesting that they did not perceive risks when contracting with unknown partners. Managers may accord ‘normal’ contracts to relatively unknown partners but we should note that these initial contracts (or bets, Coleman, 1990) were not of a nature to threaten the existence of the focal firm. Trust was offered, confirmed and reinforced when the sub-contracted firm returned the gift of trust with the offer of work at the correct level of profitability as discussed above. By returning the favour of being chosen as a subcontractor with more work, the subcontracted firm reinforced social bonds and increased interdependencies between the two firms. Creating interdependencies where individual objectives overlap ensures trust (Hardin, 1992). In game theory terms, district relationships move towards a positive equilibrium where it is in the interests of each player to honour trust and play the game according to rules which have proven their efficiency.

This exchange-based trust is illustrated by the conflict management modes employed by managers. Suppliers represent critical elements of a bar-turners’ competitive advantage. Managing supplier relationships with indulgence and ilunga in order to maintain competitiveness and ensure profitable future opportunities is a perfectly rational strategy. Local norms (honesty, offering living margins) are mobilised as means to an end. There is a culture of forbearance and cooperation in districts not because bar-turners are altruistic or naïve trustors, but because managers instrumentalise norms to achieve their own ends.

As we move in a clockwise direction in figure 2 from reflexivity to routine, these strategies have proved successful in the past and as such are handed down over the generations as ‘the way we do things here’. Norms are created through interaction (Murphy, 2006). The respect of local norms are verified and reinforced through exchanges. However, the practice of offering sub-contracting work at razor thin margins during the 2008/9 recession was possibly the beginning of a slippery downward slope where the norm of respecting one’s partner (offering a living margin) began to lose legitimacy and traction in the face of increased competition and deteriorating market conditions. Farrell and Knight (2003) noted similar
pressures leading to an increase in conflictual relations and a corresponding reduction in trust in the Bologna machine cluster. However, Barabel, Huault and Meier (2007) propose that trust is the solution to the breakdown of close ties under such pressure. In this debate of community values versus individual interest we see no reason to believe that bar-turners would choose to go bankrupt rather than reduce their margins (and offer lower margins to others). Playing the team game according to local rules (compromising, living margins) may be a perfectly rational strategy, where adherence to norms frees up cognitive resources for more difficult tasks, but managers may have to change behaviour and question past habits when local norms and attitudes become a luxury that they cannot afford.

The final interplay between antecedents of trust is the couple routine-reason where agents reflect and act on what they consider to be ‘normal’. As mentioned above a bar-turner acts in an honest way because bar-turners have no choice. Their craft does not so much make them honest but rather excludes possibilities of opportunism because bar-turners make pieces to specific dimensions. That is their role. Bar-turners work to plans provided by others; this is normal activity. Manager 11 provided talked of a counter example (the only one provided by interviewees); a bar-turner was a difficult customer and attempted to manipulate prices which served to highlight that everyone else (or the majority at last) behaves in more honest, straightforward ways. This individual is not shunned as a cheat, but is considered a ‘character’ that one must keep one’s eye on.

No better illustration of the combination of three dimensions leading to rapid trust formation could be offered than the choice of a new sub-contractor by Manager 11. Originally she chose the company (a start-up) because she recognised the type of machine they were using; knew the reputation of their former company (information); and then checked their real capacities by ordering a small, therefore low risk, trial order (process). The decision to trust was rapid. She could count on the start-up’s need for business and its need to develop business networks (encapsulated trust) and she was confident that the work would be of the necessary standard (role and reason). The start-up quickly began to sub-contract work back to the older firm thus creating a flow of business and increasing interdependence. To what extent this reversal of sub-contracting work represented a gift (Mauss, 1950:1990) is open to discussion, but the effect of this mutual ‘back-scratching’ was to create closer links between the two firms and enhance the reputation of the start-up as a player who played by the rules (reflexivity). All the actors were from the same region, born, educated and trained in the valley which facilitated
communication based on common values and thus shortened the time necessary as the actors used the early exchanges to verify that the other knew and followed the local rules.

Three factors support our central argument that reason is the fundamental antecedent to trust creation in *this* industrial district. Firstly, managers possess large amounts of information about potential exchange partners. Secondly, cognitive and organizational proximities permitted managers to evaluate the interests, motivations and expectations of their local partners because these partners were the same as them. Trust is not born of the fact that we are the same, but because being the same, we share a world view and expectations, thus making the calculation of motives easier. Finally, we can see in the conflict management modes employed by bar-turners, proof that local partners, being sources of competitive advantage, are managed accordingly, with an emphasis on compromise in maintaining long term partnerships.

Indulgence, sharing and ilunga place more emphasis on the agency of the managers involved in the conflicts and less importance on the role of internalised norms and values. Equally, the transparency and interdependency elements discussed above contribute to a reason-based construction of trust. Although Bachmann and Inkpen (2011) would consider reputation to be an institution, we must take into account that managers considered any dishonourable practices on their part would be immediately known throughout the district. Small numbers in local networks means that reputational effects are strong.

Our emphasis on agency questions Putnam’s (1993) and many district scholars, deterministic and path-dependent argument that a long history of cooperation (‘horizontal bonds of fellowship’, 1993:107) in central regions of medieval Italy lead to norms of collaboration and compromising in Italian industrial districts.

**Conclusion**

Despite the central role given to trust, there are few empirical studies on the mechanisms that lead to trust creation in industrial districts. Our contribution is to systematically investigate the creation and development of trust-based exchanges in industrial districts by employing Möllering’s (2006a) trust model which begins unravelling, as far as is possible, an admittedly complicated phenomena according to three approaches or foundations: reason, routine and reflexivity.
Our results and analysis confirm the existence of high levels of trust in the Arve Valley industrial district. District managers are in a unique position to benefit from the combination of the three antecedents of trust. Each pairing of antecedents reinforces the other in the unique environment that is an industrial district. Institutions are created through a dynamic social process which combines the actors’ bounded rationality as well as attitudes and visual clues (Murphy, 2006). Reason and reflexivity combine to allow verification of motives, expectations and what constitutes the ‘possible’ and ‘normal’.

Where we differ from many authors in the industrial district field is in the place and importance of agents’ evaluations of trustworthiness rather than any ‘blind’ adherence to locally generated norms (and it should be remembered that trust in itself is not a norm). Information flows are very high in districts thanks to cognitive and organizational proximity which is reinforced by observation from geographic proximity and frequent face to face contacts. District actors would possess ‘above average’ information about potential partners’ trustworthiness and base their trust decisions on this information. Relationships between bar-turners and local suppliers are generally trustworthy because, information flows, reputation effects in small networks, encapsulated trust and the shadow of the future all contribute to the logical appraisal by bar-turners that trust will be honoured. Although Bachmann and Inkpen (2011) would consider reputation to be an institution, we must take into account that managers considered any dishonourable practices on their part would be immediately known throughout the district; following norms to preserve reputation is in itself a rational strategy.

Further evidence arguing for a predominance of reason based trust creation comes from the conflict management modes used in intra-district exchanges. The indulgence, sharing and ilunga demonstrated by bar-turners place more emphasis on agency and less importance on the place of internalised norms and values.

The primacy of information processing in trust creation, despite its obvious flaws, is a logical extension of the view of the district as a transparent community market (Maskell and Lorenzen, 2004). It reflects the place of information flows, both tacit and explicit, at the heart of any explanatory theory of economic agglomeration (Maskell and Malmberg, 2007).

Although information and knowledge lie at the heart of this literature stream, it has yet to penetrate the examination of trust in districts. Few authors have taken trust as a central theme in their research and most district literature treats trust as a path dependent cultural trait built up over years of face to face interactions. Industrial districts, being widespread but uniquely
structured productive systems which ‘manufacture’ trust are fertile ground for further study of trust creation. Further research in this field could examine the notion of ‘embedded agency’. Of great interest is the dialectic between institution creation, reproduction and diffusion, and trust decisions made inside these institutions which themselves may or may not be recognised as such and thus, questioned by the agents involved.

Dietz (2011) suggests that the information processing model, including feedback loops permitting verification of hypotheses, is universal and common to all contexts and cultures, or emic (Saunders, et al., 2010). It is not in the remit of this paper to examine the question of universality of Dietz’s model. It is possible, however, that district managers may be trusting along calculative lines because of their unique position and context. They possess large amounts of information about very similar exchange partners; allowing them to evaluate partners’ motives and they recognize the strategic importance of close local ties.

Practitioners in districts and other contexts could reflect on the manner in which they allow, create and control information flows with prospective partners. Openness and transparency may not come naturally to many SME managers but information which allows a partner to evaluate one’s own trustworthiness (rather than trying to evaluate the other’s trustworthiness) could increase the chances of creating trust. It is the same with reputation management. While being concerned with one’s reputation is not a new concept, rapid information transfer in districts magnifies its importance because possible partners would learn of transgressions sooner rather than later. It is more difficult to propose managerial implications with the second pillar of reason based trust, interdependency, because of its more firm-specific nature. Managers looking to create interdependencies must systematically evaluate the strategic importance for the other firm of a particular project, transaction etc. An evaluation which is made easier in districts because of such high levels of homophily.

In summary, this paper contributes to trust and industrial district literature in three ways. Firstly, we demonstrate how actors display more agency and rationality in creating and maintaining local ties that are critical to their firms’ competitiveness. Trust decisions are taken, to a large degree but not entirely, through a calculation of costs and benefits which are directly related to the trustee’s perceived interest in maintaining good relations in the future. This decision is aided by large amounts of salient information in currency in local social and business networks and the expectation that the prospective partner will play by the rules. Managers making trust decisions seem to assume that local partners know and will abide by
these rules because the (local) partner is not so different from themselves. Nevertheless,
decisions are not taken blindly - reputations and competencies are commonly checked during
initial exchanges.

A second contribution which reinforces our view that managers do not blindly follow deep,
historical ‘traditions’ of trusting behaviour (as per, for example, Italian district research), is
the way in which they manage critical local linkages in ways that we could only describe as
indulgent. Opportunistic behaviour on the part of a (local) supplier was considered unlikely
until problems occurred at least three times (resonating ilunga). Furthermore, the relationship
with suppliers was maintained by generous behaviour which involved gift-giving in
negotiations and a distinct reluctance to take advantage of stronger market positions. Finally,
our third contribution is the analysis of the interplay of the three foundations of trust in the
creation of close ties. Each of the three factors reinforces the others, and this underpins trust
creation in industrial districts.
### Appendix 1

<table>
<thead>
<tr>
<th>Manager</th>
<th>Company Type</th>
<th>N° Employees</th>
<th>Date</th>
<th>Duration</th>
<th>Remarks</th>
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<tr>
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<td>Outside owner</td>
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