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# The Role of Social Capital in the Industrialization of the Food System: Comment

Stephen M. Smith

I found this paper to be quite interesting and thought provoking, which is the norm when Allan Schmid is involved. For years, he has provided our discipline with considerable intellectual stimulation. There is a lot of “meat” in the paper, and I will not be able to address all of it in the limited space. What I would like to do is (a) put this issue in the context I use in a graduate class to show where I think social capital fits in the standard economic concepts, and (b) emphasize some of Schmid’s points.

As economists, we are constantly interested in what drives economies and firms. What are the factors or inputs that affect (increase, improve) the efficient output of a firm or growth of an economy? Figure 1 shows the formulation we traditionally use to portray the growth of an economy and, without too much stretching, also can use to portray the output of a firm. There are three broad categories of factors—capital, labor, and technology. Clearly, all three are important, but in our capitalist, market-driven economy, much of our policy focus and academic interest centers on the capital aspect.

While this is a simple formulation, we are increasingly finding that the “*K*” which drives economies, communities, industries, and firms is multi-faceted and complicated. We now identify several categories of capital. Historically, the initial focus was on the physical capital, both public and private (which certainly embodies technology). To create the physical capital, however, financial capital is necessary, par-

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This is a comment on an invited paper presented by A. Allan Schmid at the Northeastern Agricultural and Resource Economics Association annual meetings, Bar Harbor, Maine, June 2001. The full text of the invited paper (authored by Lindon J. Robison, A. Allan Schmid, and Peter J. Barry) appears as a published article in this *ARER* issue.

$Y = f(K_i, L, t),$ <p>where</p> <p><math>Y</math> = the output of an economy or firm</p> <p><math>K_i</math> = physical capital, financial capital, human capital, institutional capital, and social capital</p> <p><math>L</math> = labor</p> <p><math>t</math> = technology</p>
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**Figure 1. The role of capital**

ticularly for private physical capital. Human capital (education, skills) is by now a well-accepted focus with considerable investigation underlying it. Institutional capital has not benefitted from much investigation within the standard contexts, but can be considered to comprise such institutions as the education system, public services, laws, and business. Social capital is the most recently identified facet of capital, and “mainstream” economists are incorporating social capital into their research on economic growth and development, as well as on business organizations (Rupasingha, Goetz, and Freshwater, 2000; Woolcock, 1998).

So, in the context of the formulation in figure 1, which of these aspects of capital “drives” economies and firms? On which do we, or should we, focus our analysis and policy? To the extent we do not include all of these arguments or factors, what will we miss with respect to maximizing the social welfare function? effective public policy? or the efficiency of a firm?

What do Schmid and his co-authors want us to come away with? to show us? to make us think

about? First, their context is market theory assumptions versus realities. They point out the “market” has changed, from one dictated by supply and demand, leading to a price, in an auction context, to one where price is one aspect, but it is controlled (within bounds of costs and profits), leading to other aspects having equal importance in production, processing, and distribution decisions.

Second, the new context also is one that is much more global, for both markets and individual firms. The authors see our economy and the business world as increasingly consolidated and coordinated—perhaps the “supply chain” about which we hear so much. And this coordination is motivated by a series of factors they identify. To quote them,

The irony is that such coordination developments tend to involve movements away from the pure spot market-driven concepts of economic competition, with replacement by the various contractual arrangements which depend heavily on the integrity of the transaction parties, building of trust, creation of effective incentive systems, sharing of information, monitoring and enforcement arrangements, and other factors. Some have argued development depends on moving away from relationship-dependent outcomes. But in an environment where fewer and fewer firms are absorbing increasingly high levels of risk, it may be that increasing dependence on social capital is an appropriate response to risk.

A related, or supporting view (by non-economists) of this globalization of business is that it is not a logical process, but a socially contested one; and it is not something that is disembedded from particular contexts or places. In this view, the global reach of business depends upon intricate interweavings of situated people, artifacts, codes, and living things, and the maintenance of particular tapestries of connection across the world (Whatmore and Thorne, 1997). The authors maintain it is networks that govern this process, and that networks, unlike machines, are not self-sustaining.

Thus, in this changed context, Schmid and co-authors have identified a key issue in the changing nature of our economy and businesses which underlies behavior. Price signals are not the only crucial factors governing decisions and providing incentives. In this context, Malecki (2000) identifies three ways that social capital facilitates market transactions: (a) through the creation of a system of generalized reciprocity; (b) through the establishment of information channels, which provide sorted and evaluated information and knowledge; and (c) through the simplification of market transactions by insti-

tuting norms and sanctions by which economic exchanges can occur, thus bypassing costly and legalistic institutional arrangements associated with market transactions.

If the market, as standard theory portrays it, is no longer the [only] governing force, then how do we operate as economists? How do we analyze, or manage businesses? If we do not account for social capital, what do we miss? What will we not predict correctly? To the extent social capital is important, then as advisors to business and government, we will not give correct advice if we do not analyze its role.

Schmid raises another issue that creates a large and long-term research agenda. If social capital is a “good,” or a factor of production, then how can it be created? How can or should an organization invest in social capital, and thus generate greater productivity?

Schmid and his co-authors raise several other issues I think are worth emphasizing:

- It seems they are saying that relying on the “unfettered market” (or maintaining that the theoretically pure market is the governing context) in the modern reality will lead to both poorly functioning businesses, and to poor analysis and advice on the part of economists.
- Agricultural economists’ contributions to understanding and predicting outcomes of the industrialization process will be improved if we include in our observations and calculations a newly recognized resource—social capital. This implies broadening our models, and/or working with other disciplines.
- What we expect to be learned from models which include an expanded set of goods is that social capital is an essential resource for maintaining willing participation over time and realizing human potential. This means the parties need to invest in creating and maintaining social capital, just as in any asset.
- Without considering social capital, or socio-economic goods, then businesses in this evolving system will not be successful. Or at least those businesses and organizations electing to develop and maintain social capital will be more successful. In particular, absent relationships of sympathy and trust, the industrialization process will be stymied.

In conclusion, I think Schmid and co-authors have set up a direct challenge to the march to the free market that has gained a greater following in the last 15–20 years. They are challenging us to ask whether looking at everything through the “pure market” prism will provide us with the tools to analyze behavior and predict the results of change.

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