

VALUATION OF SOCIAL CAPITAL

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Synopsis

The concept and relevance of Social Capital has been understood and leveraged in India from times immemorial by virtue of the teachings enshrined in our ancient holy books. Research implies that the benefits from social capital derive from its development of connections between people, the “social networks and the norms of reciprocity and trustworthiness that arise from them . Their “underlying cooperation and collective action for mutual benefits and creates the basis for economic prosperity.

The Perspective

Since the foundation economists have been carrying out extensive research in an attempt to explain the process of development of countries and how a country can achieve economic prosperity. Several determinants have formed the basis of such studies. In 1957, American Economist Robert Merton Solow stated that the classical view perceives labor and capital as the main factors which affect the level of development within a nation, and economic growth rests on this theory as well. Since then many studies have been conducted to trace the effect of capital on economic growth.

It is generally believed by economists that innovation, research, and education are the main determinants affecting the capital formation and their relationship with the development of a country. A new line of study tries to explain the other hidden factors which lead to a nation with similar endowments developing faster than others. Researchers have not realized the impact of social organizations, networks,

institutions, cooperation, and trusts among individuals to elucidate these growth differences amongst countries, commonly termed as ‘Social Capital’. Social capital promotes economic growth by stressing the importance of cooperation and trust within institutions, companies, and the state, as well as between individuals.

Whether social capital impacts the growth of a country or not? This question has been part of many inflamed conversations amongst various economists recently. Research is now deviating from the belief that the growth of a nation can only be explained by the traditional inputs such as capital, labor, and natural resources. This paper analyzes the relationship between social capital, economic performance, and the development of a country.

What is social capital?

The concept of social capital has been around for decades, making a relevant impact in many disciplines. Yet this concept lacks a universal definition that could describe every aspect of it. In economics, social capital is a relatively new line of

study. Most Economists have used words such as trust, networks, or shared actions to define what is social capital. The most honored definition among scholars is “anything that facilitates individual or collective action, generated by networks of relationships, reciprocity, trust, and social norms.”

The term *Social Capital* has been used in many different ways for a long and became widely popular by the late 1990s. As per Oxford Dictionary, Social Capital is defined as: ‘The networks of relationships among people who live and work in a particular society that enable the society to exist and be successful.’ With the presence of shared identity, trust, cooperation, norms, values, and reciprocity, various social groups function effectively to produce public goods for a common purpose.

According to the OECD (Organization for Economic Co-operation and Development), social capital is defined as: ‘networks together with shared norms, values, and understandings that facilitate co-operation within or among groups.’ Social capital like human capital or

labor is a very critical facilitator, However, social capital cannot produce economic growth on its own. Thus, considering social capital as either substitute or complement for various other types of capital is the most viable option. The reason for this consideration is quite simple: in times of lack of access to financial capital, social capital can act as a substitute by making it possible for individuals to rely on close relationships, such as family and friends.

Types of Social Capital

Social capital can be categorized under two broad perspectives, namely: The network perspective and the Social Structure perspective.

Network perspective: From a network perspective we can classify social capital into 3 broad types,

- **Bonding Social Capital:** Bonding ties relate to a high degree of network proximity among individuals belonging to the same group. It is correlated with norms and trust between the local communities, where people in the community tend to know each other.
- **Bridging Social Capital:** Bridging ties operate by the way of formal hierarchical structures, or more formally it relates to the vertical links between individuals of distinct social groups. Due to its power of networking outside normal circles, Bridging social capital offers a variety of individual and group benefits to people.
- **Linking Social Capital:** The linking social capital works on similar lines as bridging social capital. It describes norms relating to networks and respect for the relationship among people who interact across formal or institutional powerful authority in society.

From this viewpoint, we can get

three types of social capital, however conceptual ambiguity of each of these types leads to further complications while measurement.

Social structure perspective: Under this viewpoint, we can categorize social capital based on structure, source, and cognitive forms. Description of each of them is as follows:

- **Structural Social Capital –** Structural social capital points towards various properties of the social system which helps in the formation of social organizations in a society. It also aids in laying down certain rules, precedents, and procedures, while encouraging collaboration, exchange, and interaction between people.
- **Cognitive Social Capital –** Cognitive social capital is associated with elucidating the proper way of acting in social culture, directing individuals to collective actions. A common understanding of shared language and a shared sense of belonging is predisposed when communities tend to share values, norms, and beliefs.
- **Relational Social Capital –** Relational social capital connects with the idea of the personal relationships shared by people. These relationships are stand on the pillar of trustworthiness, identity, norms, sanction, obligations, and expectations.

Impact of Social Capital on Organizations

A) Value from Internal Social Capital:

Businesses should expect investments in building their internal social capital such as providing an environment where norms and values are adhered to or encouraging networking relationships among

employees in the company to provide:

- **Improved Financial/Strategic Performance :** Social capital in the form of structural, relational and cognitive, either independently or jointly provide value to organizations in the form of increased profitability, sales growth, and increases in market share. These are achieved by way of cost reductions, and improved awareness of the organization's products from social capital actions as explained in detail in other portions of this report.
- **Efficiencies :** The efforts that a business expends in building trust, goodwill, and high levels of formal and informal collaborations among members of the company will reduce the reliance on cumbersome monitoring procedures, thereby lowering the transaction costs associated with accumulating knowledge from internal transactions.
- **Enhanced Innovation :** The trustful relationships between employees in a company can speed up information flows and knowledge exchanges because of the decreased need for controls. This can increase the innovativeness of the organization and lead to product development, process innovations, and technology adoption, which the organization can use to differentiate itself from other competitors.
- **Enhanced Competitiveness :** Social capital helps to combine human and intellectual capital in organizations into human capital bundles that competitors might find difficult to imitate, by creating the friendship and professional ties between talented individuals that bind knowledge workers

to the company and enhance information sharing and knowledge creation. These can be exploited to increase the implementation of strategic initiatives within the firm and enhance the company's competitiveness.

- **Improved Operational Performance** : Workers who exhibit great loyalties to their colleagues are less likely to leave because the social connections with co-workers are firm-specific and relatively immobile. Ties are typically much stronger between employees than between employees and the employing company. Thus, a firm that is able to create social ties among its key knowledge workers may be able to reduce employee turnover significantly and thus enhance quality and also reduce costs.
- **Project success** : Social capital contributes to knowledge integration among teams within a project implementation environment. The historical relationships and the ties developed among team members facilitate access to broader sources of information, and information's quality, relevance and timeliness, and thus enhance the level of coordination and interactions with colleagues and contribute to project success.
- **Facilitate change management** : High levels of trust between leaders in a firm and other members of the firm will permit the transfer of sensitive information which will then enhance collaborative action within the organization, thereby diminishing resistance to change.

B. Value of External social capital.

Businesses should expect investments in building their external social capital to provide:

- **Cost Reductions** : The relationships a firm develops with its suppliers, customers, and even competitors can lead to reductions in transactions costs such as unnecessary documentation, monitoring procedures or reductions in contract enforcing mechanisms, leading to cost savings for the firm.
- **Sales Growth** : Social capital in the form of networks will allow businesses to identify new market opportunities, obtain strategic resources and gain legitimacy from external stakeholders, which leads to market share advantages and growth in sales.
- **Reputation** : Organizations might encourage their workers to collectively engage in volunteer activities within the communities in which they operate such as leveraging the resources of an organization like Habitat for Humanity to build a house for a needy family. Such goodwill within the community might provide benefits to the organization in the form of enhanced reputation, 'license to operate within the community', and protection of the organization's property in the event of civic unrest within the community.
- **Contribute toward employment growth and gain valuable employees** : A firm might, through its relationships with the community, provide educational opportunities to groups in the locality using the expertise of its workers. The educational activities might be in the form of developing entrepreneurial know-how,

formulating business plans, basic accounting, financial management, or time management.

- **Mitigate effects of poor strategic/operational decisions** : A poor location decision by a firm such as in the case of a hotel can be mitigated through networking relationships (e.g. closeness, local efficiencies, linkages with agencies, commercial agreements) with other companies in the same geographical area to increase occupancy and revenues.
- **Increased shared value** : A thriving community contributes to a successful company. The mobilization of a company's resources and the leveraging of those resources with other community resources to improve the overall health, well-being, and improvement of socio-economic welfare of the community, which reduces risks of protests and pilfering. Empowered community members may then choose to become consumers of the company's products and services. The company also benefits from reduced crime, safety for its employees and their families, and protection of its property.
- **Improved sustainability of the company as a member of the ecosystem** : A company has practices, procedures, guidelines that enable them to comply with laws, standards, and even minimize the use of natural resources (e.g. water, energy, materials).

Understanding and measuring social capital will:

- Provide opportunities for businesses to explore the benefits of both formal

relationships (e.g. established relationships between a business and its suppliers or the government) and informal relationships (e.g. relationships or engagement between a business and community leaders).

- Enable communities to identify the benefits that can be derived from the trust, norms and value systems that exist within organizations
- Provide opportunities for businesses to use the connections and relationships they develop with communities to create social change, inculcate the idea of sustainability, and address the social needs of communities.

Value creation is the essence of effective company strategies and the primary source of their competitive advantage. It has been argued that the source of this advantage is the ability to develop intense social capital, which facilitates the creation of intellectual and other forms of capital and, from that, new value. Social capital can contribute to economic growth through the accumulation of human capital. Further, it can assist economic growth through financial development resulting from, for example, collective trust between a company and its suppliers that leads to reduction in transaction costs (less monitoring of supplier quality) or from adherence to shared norms and values within the company that leads to efficiencies. And finally, social capital contributes through the networking and collaborative activities of firms that lead to the creation and diffusion of innovations.

How can a Business assess the value of Social capital

The value of social capital is not easy to assess because the benefits are not always tangible. This often requires that proxies be used in

assessing the impact of social capital. Furthermore, the impact of any social capital investment such as fostering trust, civic engagement activities, networking relationships are not always direct but occur through other intervening mechanisms such as human capital development or the strategic orientation of the company. This is even truer when a company tries to assess the societal value of its social capital activities given that that social value might be dependent on numerous other underlying factors.

The value of social capital is not easily assessed. However, the inability to assess its value should not diminish the 'capitalness' of social capital. Social capital value has effects that persist over time and thus investments in social capital should recognize the long-term benefits of the investments. For the individual, social capital has the potential to increase job opportunities, lead to income, and improve health, among others. For organizations, the benefits of social capital include the potential to decrease costs, open up markets, gain access to resources, and improve innovation capability, which can then be translated to monetary value.

Three activities are necessary in order to turn social capital into value-adding community, organizational, and individual performance. These activities are (i) establishing a shared vision among all stakeholders, (ii) measuring and reporting the value added by social capital, and (iii) building a supportive social ecosystem. Assessing the value of social capital requires consideration of the context in which the social capital occurs. Moreover, there is a wide gap between how social capital has been defined and how it has been measured in different environmental and disciplinary contexts. Thus, there is still a challenge in identifying and using uniform indicators in measuring social capital because of its contextual nature.

Before embarking on the creation

of a questionnaire to measure social capital, it is essential to take the time to reflect on your organization and its activities: why is the concept of social capital relevant? This reflection will help understand how the concept of social capital applies in the organization's specific context, and target, in the development of the questionnaire, activities likely to produce social capital. It will also help select questions that relate to the most pertinent types and factors of social capital generated by these activities.

Appropriate the concept of social capital according to the organizational context

- Identify the reasons for measuring social capital
- Identify the activity or activities likely to generate social capital
- Choose the most appropriate time(s) to distribute the questionnaire
- Determine the target population for the questionnaire
- Select the tool(s) to distribute the questionnaire
- Construct the questionnaire
- Write an introduction
- Select relevant questions
- Adapt questions
- Determine the order of questions
- Test the questionnaire
- Modify the questionnaire as needed
- Distribute the questionnaire
- Select the methods for distributing the questionnaire
- Analyze data
- Identify the response rate
- Analyze responses to each question
- Produce cross-analyses (if the number of respondents is sufficient)
- Interpret results

- Disseminate results : To the population targeted by the questionnaire, Within the organization Outside the organization

Use different measures for distinct dimensions of social capital (structural, relational, and cognitive). This will enable the impact of the various dimensions of social capital on individuals, organizations, or communities to be clearly identified so as not to mask their value.

- When measuring social capital, distinguish between the sources or inputs into social capital and the outcomes from social capital.
- Social capital value persists over time and thus investments in social capital should recognize the long-term benefits flowing from them.
- Recognize the importance of context when measuring social capital. The value of social capital depends on the context in which the social capital actions occur. A company might encourage its employees to participate in civic activities in their communities and this might enhance the reputation of the company within the locality. However, in another community the same engagements might yield different outcomes.

The abstract nature of social capital and difficulty in agreeing on its definition poses a challenge to universal means of measurement. Measurement of social capital depends in part on the way in which it is defined, conceptualized and applied to social phenomena. The approaches used to measure social capital also depend on the disciplinary focus of the measurement (e.g. economics, sociology, management, health, etc.), the dimensions of social capital (structural, relational, and cognitive),

and the level of analysis (individual, group and organizational, community and national)

Research suggests that the measurement of social capital reflects a multidimensional nature, and the various components could be summarized into four broad categories:

- Networks, relationships and connections
- Trust
- Civic engagement and voluntary activities (including cooperation, political participation, social participation, associational memberships, community volunteerism, etc.)
- Civic norms, shared norms and values

Commonly used measures of Social capital

These are measures that have been used effectively to measure social capital by researchers and international organizations interested in assessing the role of social capital in the creation of value for companies, institutions and communities. These measures could easily be adopted by a company to assess the extent and quality of its social capital.

- **Network structure**
 - ▲ Examine the diversity of the networks of employees of the company. Diversity refers to differences in ethnicity, gender, age, educational background etc.
 - ▲ Examine the size of the networks of the employees of the company. Size is the number of people who are connected to the employee.
- **Relationships, ties and connections**
 - ▲ Examine the closeness and quality of the social

relationships, connections and network ties individual employees have with their colleagues.

- ▲ Examine the closeness and quality of the social relationships, connections and network ties managers and employees have with the company's key external stakeholders such as customers, business partners, suppliers, community leaders, and government officials.
- **Institutionalized and Interpersonal trust**
 - ▲ Examine the degree to which employees in the company trust what the company stands for.
 - ▲ Examine the degree to which employees trust government agencies, the business environment, communities, etc.
 - ▲ Examine the extent to which employees trust company executives and other employees.
- **Associational membership**
 - ▲ Assess the degree to which individual employees are members of professional and community organizations and associations.
 - ▲ Assess the number of associations/ organizations in which individual employees are members.
 - ▲ Assess the number of times individual employees get involved in associational activities in a specific time period (e.g. monthly)

Tools for measurement of Social capital

Use surveys, interviews, focus

groups, and personal stories from employees, members of a community, or stakeholders to implement

- World's Values Survey's Social Capital Index
- Network structural characteristics (e.g. density, diversity, size, etc.)
- Social relationships and ties
- Company codes of conducts and values
- Putnam's Social Capital Index Survey Instrument
- World Bank Integrated Questionnaire for the Measurement of Social Capital (SC-IQ)

Concluding notes

Social Capital is defined as: 'The networks of relationships among people who live and work in a particular society that enable the society to exist and be successful.' With the presence of shared identity, trust, cooperation, norms, values, and reciprocity, various social groups function effectively to produce public goods for a common purpose. Social capital started more as an academic notion, has over the last few years been used and applied vigorously to many valuation exercises.

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