

How much will you pay for an idea?

by

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A few weeks back I extolled eBay's seller and buyer reputation system as a model upon which many professional service associations might base themselves. The idea was that by having a clear means of providing positive or negative feedback, individual providers would have scope to invest in their reputations. This could be for workmanship, fair dealing or any qualitative aspect of service.

I based that opinion on little more than my own experience of eBay and the general dilemma's faced by individuals trying to build a reputation. Fortunately, since then, eBay has provided a vehicle by which the value of reputation can be quantified.

Professors Luis Cabral and Ali Hortascu from New York University and the University of Chicago respectively have studied how eBay's reputation system is utilised by sellers. Because of the transparency of eBay's system, this is one situation where the researcher can have almost as good a picture of an individual's reputation as traders themselves.

Here is what they found. First, in theory, seller's who have built up a good reputation will be more motivated to engage in selling. Specifically, they might choose to engage in a greater number of transactions. Conversely, having built that stock, if they were to receive a negative rating on one transaction, this might be demotivating. And this is precisely what happens. The growth rate in a seller's transactions is, on average, 7 percent before the negative rating and -7 percent afterwards. Also on the effort side, having had one black mark against them, a seller is twice as likely to have more black marks than a seller with a clean slate.

Second, in theory, a good reputation should be valuable. And indeed it is. Cabral and Hortascu found that sellers with good reputations earn more revenue. Increasing your negative feedbacks as a proportion of your volume of trades by just 1 percent leads to a 9 percent fall in your revenue. Clearly, this will be a real worry for high and low volume sellers alike.

Given this, it shouldn't be a surprise, if sellers with a bad reputation stop selling or at least (and it is hard for researchers and others to observe this) come back in a different guise. Sellers who trade 10 times more than the average, have a much lower chance of pulling out (around 25% less). However, a 1 percent rise in negative feedback only increases the chance of pulling out by a modest amount. So the picture seems to be that sellers would prefer to build up a record of transactions and withstand some black marks rather than give up the ghost entirely.

Finally, it is interesting to think about how sellers build up reputations in the first place. It turns out that on eBay a good way to do this is by being a good buyer first. After all, trustworthy buyers are also likely to be trustworthy sellers and not skip out on deals. About 30 percent of all sellers appear to start predominantly with buyers and these folks generally have a higher reputation as sellers. So perhaps trust is 'in the blood' and we only need to discover its colour for the system to work.

To be sure, this is a snapshot of the value of reputation and trust. But it does give as a picture as to the potential value of this. Imagine how valuable a clearly solid reputation is in an environment that isn't as transparent as eBay.

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