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Social Capital Formation in Australian Rural Communities: the enhancing role of the stock and station agent

Simon Ville

University of Wollongong, sville@uow.edu.au

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Abstract

Evidence from the Australian stock and station agent industry is used to examine several unresolved issues of type and measurement in the social capital literature. Two distinct types of social capital are analysed from the evidence, one being long term and innate to a community, the other variable in the shorter term through individual decisions. The two types are causally linked, innate providing propitious conditions for individual investment conditions. Social capital investment is measured through the proxy of goodwill as revealed in takeover analysis.

Keywords

social capital, goodwill, rural communities, economic history

Disciplines

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Social Capital Formation in Australian Rural Communities: the Enhancing Role of the Stock and Station Agent¹

Introduction

We look at an Australian industry in which social capital featured prominently and use this evidence to address several conceptual and methodological issues in the social capital literature. The growing literature provides no consensus regarding social capital's determinants; whether it is intrinsic to a community or subject to engineered change by individuals or entities. A second issue is the measurement of social capital. Various methods have been suggested but no consensus reached. We suggest a new approach for measuring a particular type of social capital, that embodied in the decision-making processes of firms. The historical focus of the paper is the Australian stock and station agent industry (hereafter 'agents'). Agents have been an important part of Australian rural communities since the mid nineteenth century, providing financial, marketing, and technical services to primary producers, particularly wool growers. Their success depended heavily upon the prevailing level of social capital in the community, and their ability to enhance this with planned investments that provided additional economic returns both to agents and to the rural community. We will describe the sources of social capital in colonial Australian rural communities, analyse the additional investments made by agents, indicating how these changed over time, and measure the scale of their investments.²

The different guises of social capital

Extrapolating from a large conceptual literature, social capital is defined here as the development of shared social norms and values based on cooperation, trust,

reciprocity, and obligation. Bourdieu and Coleman in the 1980s presented social capital as the product of individual decisions ('purposeful actions') but much of the subsequent literature, particularly as a result of Putnam's work, focussed upon social capital as a community attribute. Recently, Glaeser, Laibson and Sacerdote returned attention to the individual, developing a strategic model of economic behaviour that incorporates intrinsic abilities and deliberate investments. Sobel helps to reconcile the two strands of thought by interpreting social capital as, 'an attribute of an individual that cannot be evaluated without knowledge of the society in which [he/she] operates'. In other words, the individual's decisions are influenced by the prevailing set of attitudes, networks, and relationships in a community. However, Portes notes that 'the two definitions of the concept, though compatible in some instances, are at odds in others'. In particular, the two concepts are in tension when an individual's social capital investment weakens that of others or the community: for example an individual may use privileged social connections to queue jump, or, expressed formally, pursue goals that lead to a pareto suboptimal redistribution. The work of Ogilvie on European Medieval guilds provides evidence that social groups can lead to exclusivity and rent seeking behaviour. We investigate an historical example in which individual and community social capital reinforce each other to the benefit of agent firms and local pastoralists. We label these two forms of social capital as 'innate' (intrinsic to a community) and 'planned' (engineered change by individuals or entities).³

Social capital in Australia

While there has been no systematic attempt to measure stocks or flows of social capital in Australia, several recent studies of community organisations present a

picture of a nation of ‘joiners’, rather like Putnam’s United States. Keen surveys the rise and decline of Mechanics Institutes, Friendly Societies, Women’s associations, and service organisations. Mechanics Institutes, based on the British form, grew up from the 1830s to provide educational learning and social interaction but declined after World War One in the face of competition from the commercial and public sectors. Friendly Societies provided collective support in sickness and death, covering as much as 46 per cent of the New South Wales population at their peak in 1913. Women’s organisations grew up from the late nineteenth century to support causes such as temperance and female suffrage. Service organisations, most notably the Rotary Club (1921), have addressed issues of social deprivation.⁴

Australian organisations often drew upon similar activities prevalent in Britain or the United States, either through direct participation or observation, confirming the international transferability of social capital previously identified by Greene and Khan. In contrast to Putnam’s story of secular decline in the United States, however, Keen identifies cyclical trends in Australian associational activity arising from and positively correlated with fluctuations in the level of economic activity. Evans in a cross-sectional study of 2001-2 concluded that Australians continue to have among the highest rates of participation in charitable organisations worldwide and that Putnam’s thesis is unproven for Australia.⁵

Rural communities

Onyx and Bullen’s 1999 survey found higher levels of social capital in two Australian rural communities than two suburban and one city location, particularly in relation to trust, safety, and participation. Evans, likewise, found that levels of community activity in Australia were higher in rural than urban locations and that

individuals with a rural upbringing tended to maintain a higher commitment to altruistic community organisations, even when they moved to a different location. Such evidence bears out the conclusions of the conceptual literature that the stock of social capital tends to be high in small homogeneous distant communities with a strong sense of internal identity and boundary, and limited mobility.⁶

Empirical studies of pre-industrial village life in Britain and small towns and villages in early twentieth-century United States point to the strength of rural social capital. An historical overview of Australian rural communities in the nineteenth and early twentieth centuries confirms a predominance of features conducive to high levels of social capital. Rural settlements were small affairs of often only a few hundred population. They were peopled by a relatively homogeneous group of settlers, educated and of medium to high social rank, who brought their experience of social capital formation from Britain. They frequently came from the same region of Britain, shared similar cultural values and religious beliefs, and included large extended family groupings. Scots, with their strong emphasis upon family and clan, were numerous. Former military officers and employees of the East India Company were also common. They shared a common pursuit of farming and encountered the same climatic, financial, and economic challenges. The long distances from, and poor communications with, other settlements and major centres emphasised the sense of internal identity, boundary, and self-containment. Investments of fixed capital and personal toil into their farms reinforced the immobility of many of these settlers by creating a relatively illiquid form of livelihood from which migration was difficult.⁷

Where ethnic, religious or social heterogeneity intruded upon the Australian rural setting, it rarely engendered distrust and dislocation. Outside the itinerant goldfields communities, European-Chinese relations were generally characterised by

‘mutual cooperation and benefit’. Lancashire has noted the support of rural institutions such as the judiciary, local press, and large landowners for their Chinese communities against prejudicial legislation emanating from urban central government. Nor was religious inter-denominationalism frequently a source of conflict, relations between Catholics and Protestants in rural Australia were ‘harmonious and cooperative’ helped by non-extreme forms of doctrinal interpretation if not a degree of irreligiosity. Similarly, social distinctions were less divisive than in Britain or the urban areas of Australia, particularly with the decline of the dominant squatter class in the second half of the nineteenth century.⁸

Rural settlements contained a plethora of community organisations of a strongly inclusive and socially interactive nature. Social and sporting clubs, charity groups, religious gatherings, agricultural and horticultural societies and farmers clubs were to be found in most pastoral and farming districts of south-eastern Australia by the late 1850s. Regular meetings and shows emphasised agricultural societies and farmers clubs as highly integrative groups. Another distinctive rural organisation was the women’s country association although the national body, the Country Women’s Association, was not formed until 1922. It has been concerned with socially integrative activities such as rural education. Social capital was additionally captured by high levels of kinship in extended families that settled together in rural towns. Finally, a tradition of informal social gatherings at festivals and fairs created a sense of community and place on which trust and cooperation could be built.⁹

Community interaction fulfilled social needs in the absence of external distractions and contacts, and facilitated economic goals through the sharing of information, equipment, and the provision of other forms of mutual support. The close-knit nature of these communities and the regularity of interaction provided a

strong promise of cooperative behaviour and a guard against opportunism through informal monitoring. As a contemporary noted, 'everyone knows his neighbour's business'. While disputes, particularly with neighbours over ill-defined boundaries, were not uncommon, the strength of trust and cooperation facilitated resolution. Victorian settler Alfred Joyce noted that disputes with his neighbours were easily resolved, 'being like ourselves of English nationality and in a similar social position'. Joyce describes the cooperative manner in which rural communities organised their own medical, religious and postal services with each family paying an annual charge based on their needs and means. Taken as a whole, social engagement provided a form of insurance against the huge uncertainties facing small agrarian settler communities. The continuation of relatively high levels of social capital in these communities today, in spite of the diminution of many of the conducive conditions (larger more heterogeneous populations, improved communications, alternative social contacts), further suggests that these early settler communities were characterised by a substantial accumulated social capital stock.¹⁰

A social capital gap?

In spite of high levels of innate social capital, many rural communities in mid-nineteenth-century Australia were in crisis and in danger of collapse. Pastoral output growth in the second quarter of the century had provided few solid foundations for their long-term expansion. There was minimal use of capital and technology due to financial constraints, and an ignorance of improved animal breeding methods due to a lack of local research and limited access to overseas sources of innovation. Simple nomadic herding, inadequate flock control, and inexperienced ex-convict overseers contributed to heavy stock losses and poor quality animals. These problems were

compounded by high turnover rates resulting from a lack of experience and resources to deal with major sources of uncertainty especially droughts, bushfires, bushranging, sheep rustling, pestilence, and periodically falling prices. Similarly, wool marketing occurred through various unsystematic channels.¹¹

Market failures help to explain the problems faced by these communities. Small wool producers encountered various challenges including the need for financial support to cover long term capital investments, short term marketing costs, and cyclical downturns in the volatile farming sector. The principal wool markets were distant from the local community either in one of the Australian port cities or in London. Finally, the farmer needed to keep abreast of commercial and technical information including changes in the relative prices of wool types and other farm products, and innovations in farming equipment and raw materials. These challenges could be met to some degree by cooperative behaviour within the community, especially the sharing of knowledge within agricultural societies and through joint ownership of capital equipment. However, rural communities were unable to provide for most of the farmer's credit needs or handle the growing complexity of wool marketing, while most commercial information was remotely sourced.

Farmers, therefore, required financial, marketing, and technical service providers with contacts beyond their community. Non-local service firms, however, were unlikely to find such business attractive since they lacked the local knowledge to make effective lending decisions, pursue appropriate marketing strategies, or offer suitable technical advice. The smallness of most farming units by the late nineteenth century, and thus resulting commissions, deterred service firms from committing the resources needed to make accurate decisions. Finally, the complexity and uncertainty of farming in these evolving communities made complete contract specification

difficult, while the enforcement of contracts and associated property rights was difficult to achieve in the absence of well established legal institutions and practices.

Therefore, the innate social capital stock, while apparently high, attained an equilibrium below the optimum for the rapid economic development of rural communities. Most writers agree that innate social capital possesses public good qualities: it is non-rivalrous in that one person's use does not prevent another's, and non-excludable in that all members of the community can benefit from it. Like many public goods, social capital generates externalities: the benefits of a trusting cooperative community extend beyond that community, an individual or firm knows of its positive reputation and can benefit from that knowledge. Externalities lead to underproduction since the contracting parties fail to capture all of the benefits. Where the production of public goods remains below optimal levels, this provides a case for government intervention to fill the gap. Governments contributed to the expansion of social capital in rural communities through the evolution of formal institutions governing property rights and the law. This was a slow process, however, and tangential to market failures originating in the remoteness of these communities and the smallness of their rural enterprises over which government had little influence.¹²

Engineering additions to social capital

The solution to the 'social capital gap' lay with the stock and station agents who were part of the rural communities but were also networked into and transacted with a wider world of national and international business including shipping companies, importers, banks, insurance companies, and equipment manufacturers. The stock and station agent industry emerged in the 1840s, consisting mostly of small local firms based in country towns in south-eastern Australia. Most agents were local

mercantile traders or farmers who saw new business opportunities in the burgeoning pastoral sector, particularly through the growth of wool exports. Frederick Dalgety, the founder of one of the industry's most successful firms, began as an importer and wholesaler in Victoria of the 1840s before turning to stock and station agency in the following decade. Like several other pioneers, he operated a handful of regional branches, each with substantial autonomy and a separate partnership consisting of Dalgety and several local entrepreneurs. It was only in the mid 1880s that he merged the branches into a single legal entity and subsequently began the process of organisational consolidation and national expansion in the following decades. Dalgety and his ilk were already connected to mercantile and finance networks and soon expanded this into insurance, shipping and equipment manufacturers through their stock and station agency work.¹³

Aware of prevailing high levels of trust and cooperation, agents engineered increases in social capital designed to overcome contractual failures by fostering a series of ongoing bilateral relationships with individual farmers based upon honesty, transparency, trust, and reciprocity. They sought to convert contingent relationships, as part of a small rural community, into durable obligations with particular farmers and their families; what the agents themselves referred to as establishing 'connections'. The extensive information flowing from this relationship enabled agents to make more effective lending decisions, offer suitable technical advice and marketing services, and mitigate the risk of default. The existence of high levels of innate social capital and the fact that many agents were already well-respected local members of the community, promised a low cost-high payoff to their investments.

The planned investments of agents provided economic benefits to pastoralists through their services and advice, thereby mitigating the market failure problems

discussed above. They additionally reinforced the innate social capital of these communities. Cooperative bilateral farmer-agent relationships signalled trust multilaterally through the community as other parties observed this behaviour. In addition, some of the agents' investments were undertaken in a broad social context such as the sponsorship of local events, awards, and organisations.¹⁴ There is very little evidence to suggest negative effects for pastoralists. Since most pastoralists used agents these were encompassing rather than exclusive social and business networks. Where agents refused to do business with a farmer or broke off the relationship, this was normally a sign to the rest of the community of an opportunist; even in hard times agents normally kept faith with their trustworthy clients.

While agents' investments were primarily incentive-based – the promise of regular income-generating business with farmers, particularly marketing commissions for handling the sale of their wool - many enjoyed the social milieu as a consumption good, and so were motivated additionally by a personal preference for facilitating community interaction and the fellowship that it yielded. On the other hand, as we shall see below, social capital investment involved substantial costs.

Forms of investment

Social capital investment by agents took various forms. The starting point was to draw upon the existing distribution of social capital by hiring local employees who were well placed to enhance trust, cooperation and reciprocity. Existing reputation and connection counted for much: local managers needed to be 'greatly respected' by local farmers and have 'much influence in, and knowledge of, the districts'. So did intrinsic attributes: a charismatic and engaging personality of standing in the community was valued alongside business knowledge, someone 'whose position also

socially admits of his talking to our clients not only in...business...but on equal and friendly terms'. A prominent branch office was then required in a central location on the main street close to the public houses, shops, and community centre. 'His office is poked away in the corner of this town', complained Australian Mercantile Loan & Finance Company of one of their Queensland premises. The siting of the office to maximise social interaction with members of the community indicates the manner in which physical and social capital investments were mutually reinforcing.¹⁵

Subsequent social capital investments took the form of time, gifts, and the provision of free or loss-making services. Such investments were either undertaken bilaterally to build a relationship with a particular farmer or more broadly to signal the firm's intentions to the community. Investments in individual relationships reverberated through the community - one of the benefits of investing in a close-knit community. Agents exploited existing social capital by targeting leading and well known farmers, aware of the 'social multiplier' effects of a good relationship with community leaders. One farmer was supported by Elders as he had, 'done quite a lot for us in the surrounding districts' and another 'will strengthen our position in the district as he has a large following...prominent position among Western Australian station owners'.¹⁶

Gift giving was intended to establish or strengthen a connection, create a sense of obligation, and test the willingness of the recipient to enter into a reciprocal relationship. Local managers were given generous expenses accounts 'to maintain a strong standing in the community'. They were used to entertain farmers at social venues and events including hotels, clubs, races, shows, and carnivals, these being regarded as an opportunity for broad social interaction away from the workplace. These included, for example, 'convivial gatherings in the back parlour of the Royal

Oak with Mr Goldsbrough [agent] and a choice company of wool and sheep men, at which, in conjunction with pipes and cards, the claret flowed freely'. Agents were active sponsors of local events, exhibitions, and competitions and invested broadly in community goodwill by supporting and providing subscriptions to local charities, cultural institutions, and even political parties.¹⁷

Agents offered some services and advice that were either free or at cost. These included advice on legal matters, business procedures including accounting and financial management, and more specific matters relating to farming practices. Again, these gifts were designed to create a sense of obligation and initiate reciprocity and trust. While its other main services, most notably produce and livestock marketing, yielded profitable commissions for agents, lending was often provided at zero profit or even loss, as agents relent bank money at or below the borrowing cost to themselves. This was motivated by the desire to obtain wool commissions in return. Agents hoped that their action would induce reciprocity from the farmer and that this would foster more harmonious relations than specifying wool handling rights in a written contract. Notions of trust emanating from credit behaviour resonate with the experience of informal capital markets in early modern Britain.¹⁸

Arguably, the most significant agent investment was of their time. They frequently visited farmers at home to build up a closer personal connection while also monitoring the condition of the property and livestock in which the agent might have a financial interest. Thomas Bostock of Strachan, Bostock made, 'yearly visits, sometimes on a bicycle, to establish personal contacts with clients, [which] were invaluable in building up the business'. Richard Goldsbrough had ridden as far as 100 miles on horseback to visit farmers. During his stay after such a long ride, as well as advising on the sheep stock, he participated in the social activities of the farmer's

family and his neighbours, including rambling, card games, and readings. 'It was of course arranged before he left us that our next wool would be sent to [him]'. Agents were among the earliest owners of car fleets, which they used to visit farmers, enhancing their corporate prestige in the process. While estimates of time committed to visits are difficult to make, it is known that some firms employed full time travellers for this purpose. Similarly, agents entertained farmers in their own home, the importance of such occasions being emphasised by the firms' preference for married managers whose wives could extend social conviviality in the domestic setting. Agents expended time acting as community advocates, using their influence in business and political circles to campaign for improved and lower cost services and infrastructure such as rail, road, telephone and telegraph.¹⁹

Enhanced internal efficiency and the decline of social capital formation

During the first half of the twentieth century, the stock and station agent industry became dominated by a handful of large firms that had expanded nationally across Australia. The number of branches operated by the five largest agents increased from around a dozen to nearly 400 and their wool market share exceeded 50 per cent. For Elders, Dalgety, Goldsbrough Mort, New Zealand Loan and Mercantile Agency, and Australian Mercantile Loan & Finance Company, national expansion was a major source of competitive advantage giving them access to a wider range of resources, facilitating risk spreading, and yielding scale economies. A more efficient and better resourced firm offered enhanced attractions to some farmers and an opportunity for cross-fertilisation between rural communities with agents providing bridging or autonomous social capital in place of the bonding version that had been embedded in single rural communities.²⁰

However, agents faced tensions between investment strategies that fostered social capital and those that maximised their internal productive efficiency. Their development of internal labour markets enabled agents to train and acculturate employees into standard company practices, who could then be moved between offices in line with shifts in corporate strategy, the opening of new offices, and internal promotions. However, Dalgety's were later to bemoan, 'we never leave anyone in one place long enough to build up a personal connection.' When the companies acquired a local firm they faced the dilemma of whether to retain existing staff to perpetuate 'connections' or replace them with transferred staff, versed in the practices and culture of the national company, rather than of the local community. Highly trained company managers with limited personal connections tended to formalise relations, replacing generalised notions of trust with specific written contracts, particularly in relation to finance and wool marketing. Thus, for example, 'moral security' on a loan was replaced by tangible collateral. This reflects a broader issue of the tendency to impose a standard company policy on all branches with little sensitivity to the different needs of particular communities. In effect, as the larger firms expanded they substituted physical and human for social capital.²¹

The shift in strategy enabled agents to offer discriminating business terms to reflect different risk levels between farmers, a policy that would have been inconsistent with the community-wide cooperation and interaction associated with social capital. Intensified competition between the leading firms and a determination to improve market share, increased the attraction of discriminating policies, such as reduced interest rates, to attract low risk clients. Product and market diversification strategies, initiated by the national agents from the interwar period, similarly shifted the emphasis away from social capital investments. The sale of a widening range of

consumer durables to an expanded range of consumers did not involve the same breadth and repetition of bilateral transactions as had traditionally occurred with individual farmers.

During the interwar economic downturn agents sought to cut costs, obvious short term targets being the gifts provided to farmers many of whom were failing to meet their debt repayments. The comments of one manager in 1930 are poignant:

We are endeavouring to curtail the expense of entertaining. It is impossible to completely disregard the custom of the...country districts where we are continually meeting woolgrowers at hotels, clubs, races, shows, and carnivals...[However] a great deal of the last three will be eliminated over the next year or two. Mr Clarke is a complete teetotaler and myself virtually...we have a natural disinclination to this method of assisting business.²²

This evidence reveals a shift in entertainment policy and also the employment of agents most unlikely to cultivate social interaction! Branches were additionally closed, weakening the connection, and so-called 'social accounts', that were unproductive but difficult to close without loss of reputation, were weeded out.

That all the leading agents successfully chose internal productive efficiency over social capital is suggestive of the net benefits to be gained. Arguably, they had previously invested in social capital above optimal levels. Local communities had developed expectations that agents neglected at the risk of losing market share. Elders noted frustratingly in 1908 'every show, church of every description, every cricket club...debating societies and even country branches of the Labor Party used to think there were special claims on us to subscribe'. Firms further reduced their social capital investments through cooperative agreements to limit these activities. Agents

were also responding to changes in rural communities, which were becoming larger, less isolated, more heterogeneous, with fewer integrative social organisations, and witnessed the growth of class-based new unionism. The resulting loss of clear boundaries and a distinct sense of identity suggest a declining social capital stock. Thus, the payoff to investing agents would have lessened. The expansion of larger scale farming businesses created a class of client less embedded in a single community and not so dependent on a broad contractual relationship with a single agent. Improved transport and communications additionally mitigated the investment of time spent on a farm visit, freeing resources for other purposes.²³

There were some disadvantages to this change of investment strategy. The breakdown in long term broad relationships with farmers meant agents were faced with more “floating clientele”, who flit from broker to broker’. As a result, they had to provide higher ratios of finance to wool clips handled in order to win this sort of business. They faced renewed competition from the larger and more efficient cooperatives that used their farmer shareholders and board members as local social capital, and concentrated upon maintaining an active country organisation through the supply of a wide range of merchandise. Most notable was Westralian Farmers whose ability to capitalise their goodwill at low cost through their country selling organisations did not go unnoticed.²⁴

Measurement

A major issue in the social capital literature is that of measurement. Comparisons of social capital between time and place can be drawn through percentages or ratios, for example the degree of trust shown by surveyed individuals or the number of counted organizations or memberships per capita in a community. It

is difficult, however, to derive a common financial unit of measurement for absolute levels of social capital for the purpose of drawing broader comparisons with, for example, other forms of capital, or with a nation's GDP.

Each measurement technique has its shortcomings. Surveys, like all direct observation techniques, suffer from the impact of the survey itself on the participant. Ironically, the willingness of the participant to cooperate and answer honestly lies at the heart of the nature of social capital! This may polarize the results - cooperators are, perhaps, likely to exaggerate their cooperation, while non-cooperators may make an issue of the lack of prevailing trust.²⁵

Membership of organizations is viewed as a manifestation of levels of social capital and, since the counting of these organizations is often possible, this has emerged as the major form of historical measurement of social capital. This was the basis of Putnam's study: the decline of social capital in twentieth century America was tracked through reduced participation in community groups. We need to assess how engaged with each other are an organisation's members: are they geographically concentrated and meet and interact regularly, or rely upon remote communication through technology. Members of a large national organization may rarely interact with one another. The ethos of particular groups may be more or less conducive to civic engagement and cooperation: welfare, community action, and environment groups may fit this picture better than political groups or professional associations.²⁶

In the last few years a broader and more closely specified range of social capital components have been developed. Black and Hughes, for example, have developed a series of components grouped under three headings. 'Patterns of processes' deals with evidence of social and civic participation; 'qualities of processes' relates to feelings such as social trust, altruism, reciprocity, and a sense of

community; 'structures that enhance social processes' specifically relates to conflict resolution mechanisms. Breaking social capital down into more discrete components may help measurement. However, there remains the problem of inaccurate counting of 'patterns' and the lack of secondary evidence of 'qualities' where surveys are not possible.²⁷

These alternative forms of measurement deal largely with innate social capital. Our focus is on planned social capital, the measurement of which has received very little attention. One approach would seek to monetise the agents' various social capital investments discussed above. However, this measures the initial and ongoing costs of the investment rather than its actual value to the company. It also presents insurmountable data problems especially for an historical study. We can only guess, for example, at the proportion of an agent's time spent building client relationships and, additionally, separating out its consumption and investment good elements. Alternatively, we might seek to measure the additional income or profits accruing to the firm as a measure of the value of its social capital investments. Again, data accumulation is problematic; how do we separate the returns on social capital from those on human and physical capital. Instead, our approach here is to measure the agents' investments in social capital through the proxy of the value of business goodwill, which provides a financial unit of measurement.

Goodwill constitutes the intangible assets of a firm, most notably patents, brands, customer base, its company name, and its overall reputation. These intangible assets reflect efforts by the firm to build a close and enduring relationship with its customers, grounded in trust and its reputation. It is these features of trust and reputation that provide a link between goodwill and planned social capital in the way that we defined the latter above. The firm that has a valued brand, a loyal customer

list, a revered name, and is well-regarded in the overall community may be said to be rich in social capital.

The connection between social capital and business goodwill has received only limited attention. Fukuyama believes that a firm's intangible assets consist mostly of 'the social capital embodied in the firm's workers and management'. However, he restricts this to the internal social relations of the firm, facilitating coordination of production, and distinguishes it from the external social capital embodied in its relationship with its customers. Sobel, though, argues that part of the social capital of a firm lies externally in its customer goodwill. Thus, taken together, social capital is reflected in both the internal (organisational harmony) and external (relations with its customers, or other external parties) goodwill of the firm, the balance between the two depending largely upon the size of the enterprise and the nature of its business. Patents are a form of intangible asset perhaps less related to social capital, whether a monopoly over a particular product encourages the building of regular customer relations or their neglect is a matter for debate.

The intangible assets of a firm are rarely evident, however, in its public balance sheet. Their value, only revealed when the firm is sold, is notionally calculated by subtracting its net tangible assets from the sale price. This 'goodwill' is then recorded on the acquiring company's balance sheet but normally written off rapidly as an asset of uncertain value. Alternatively, goodwill is calculated as the difference between a firm's market capitalisation and the value attached to it by another firm making a takeover bid. However, the difference will also incorporate the acquirer's future expectations and its perception of the value that it can add through its superior strategic management capabilities. Disentangling these factors is highly problematic. It also relies upon a rather unsatisfactory derived residual figure

methodology. Calculations of social capital based upon market capitalisation, anyhow, are of little help in a study of stock and station agents where most takeover bids were launched against private unlisted firms.

We suggest an alternative measurement using takeover information, which provides a more accurate and non-residual calculation of goodwill. Since details of the acquisition of private firms are rarely made public so as not to weaken the bidder's bargaining hand, evidence has been extracted from the archives of major agents. One of the benefits of an historical approach is the opportunity to access information that would be held confidentially by contemporary firms. The large goodwill component in many cases required the bidding firm to conduct a careful and detailed due diligence exercise to gain an accurate view of its value, which in turn provides us with robust historical data. This exercise required a knowledge of the target's client list including the current state of each account. Therefore, a successful takeover needed close cooperation between the two firms, and, indeed, many bids failed for this reason. Successful mergers often occurred between firms who had worked cooperatively in the past. Multiple bids for the same firm, over a number of years, occurred as the firms haggled over the price of the goodwill. Table 1 indicates the absolute and relative value of goodwill in eight successful takeovers in the industry between 1881 and 1947. They reveal its share of the purchase price mostly between two-fifths and two-thirds, though with extremes from 0 to 100 per cent.

Table 1: Social capital as a percentage of takeover price

Elders, well-known for its acquisitive nature, had purchased Hague's in 1937 wherein goodwill was as high as 60 per cent of the price, reasoning, 'to what a large extent the

development of the business....has been dependent on the personal work and connection'. Ten years earlier Goldsbrough Mort had failed in an attempt to acquire the same firm when negotiations broke down over the value of goodwill. In its acquisition of Wilson Bolton & Co in 1944-5, the only cost to Elders was £10 000 of goodwill, the firm leased its premises and owned no other assets.²⁸

Measuring a firm's social capital through goodwill at the point of a transfer of ownership requires the assumption of social capital's alienability on which there is no consensus. Arrow doubts whether it meets two of the three criteria of physical and human capital, including its alienability. Sobel, conversely, argues that sale of the goodwill in a business is indeed indicative of alienability. Where social capital is vested in a transferable entity, such as a firm, rather than an individual, alienability is more probable. While economists disagree on the specific question of social capital's alienability, there is growing support for, and a range of models dealing with, the idea that a company's name and reputation are tradeable assets. Tadelis, in particular, has developed such a model under conditions of adverse selection, whereby the change of ownership is unknown to the firm's clients thereby enhancing the tradeable value of the firm's accumulated goodwill.²⁹

Our evidence suggests alienability is possible, the degree of which is highly contingent on the continued use of the acquired firm's name and staff during a transitional period. In most cases, the acquiring agent paid for the goodwill of the business, to reflect acquisition of a loyal clientele. When Elders acquired Hague's in 1937, they were conscious of the alienability problem, judging that most of the growth of the business had been due to the social connections of the principal managers, and therefore sought to mitigate any loss by retaining them notionally in the new business. They were also conscious of the efforts made by Hague's to invest in the social capital

of their own organisation, fostering a positive atmosphere among their staff, which, in turn, did not go unappreciated by their customers. After Dalgety acquired Strachan Cheadle in 1906, they noted, 'Up to the present the acquisition is well received and no secession by their constituents of any importance'. In a contrasting case, in 1922 Goldsbrough Mort decided to offer nothing to Harrison Jones Devlin for their goodwill, observing 'the business is largely personal, dependent on the personality of Mr Anderson Moore, the General Manager...who is now well advanced in years'. Moore was not retained and thus social capital was considered inalienable on this occasion. It appears, therefore, that a firm's social capital was largely embodied in its name and the social relationships its employees built up with customers.³⁰

The experience of agents therefore fits Tadelis' model of tradeable reputation enhanced by hidden information (adverse selection), achieved in this case by retaining the appearance of the old firm through staffing and name continuity. In a close-knit rural community most customers of the firm may in practice have been aware of the ownership change, but the effect of name and employee retention was nonetheless to foster a sense of 'business as usual' and thus help to preserve the social capital of the firm. In due course, new employees would join the company and the name would ultimately change but this was undertaken in an evolutionary manner in which continuity was the watchword.³¹

The drawbacks of balance sheet measurements of goodwill, and through it social capital, were discussed above. However, they appear to be at their most accurate immediately following the acquisition of a company or the establishment of a new enterprise. If less reliable as an absolute measure, they facilitate a comparison of social capital's importance among a larger and mixed group of companies than can be

traced through takeover information, and enable comparisons with other forms of capital recorded on a company's balance sheet.

Table 2: Social capital as a share of total balance sheet assets in the early years of a company or following its acquisition

The social capital investment of some of the larger agents was substantial. In 1885, shortly after its public flotation, Dalgety valued its goodwill at £120 000; four years later the newly-formed Goldsbrough Mort recorded £100 000. These values were paid by the new public company for its constituent private firms to reflect their list of loyal customers. These figures were equivalent to a medium-sized Australian company of the 1880s, but were still 'much below realisable value' as Goldsbrough Mort observed. In line with normal accounting practices, both firms gradually ran down the value of their goodwill, using accumulated reserves, until it showed a zero balance by the early 1890s. Thereafter, they only showed goodwill on the balance sheets after the purchase of a firm that had included an allowance for goodwill. Subsequently, they would again seek to eliminate goodwill from their balance sheet. As we saw in the previous section, in practice, these companies continued to invest in social capital although at a declining rate as they concentrated upon national expansion through human and physical capital investments.³²

From the foregoing discussion in the previous section, we would expect to find that social capital was relatively more valuable for smaller local than the emergent larger national firms, reflecting the former's closer embeddedness in small rural communities. This is borne out by evidence from balance sheets and takeovers. Goldsbrough Mort's and Dalgety's goodwill represented only 3 per cent of their

balance sheet assets, and in the case of Elders a mere 1 per cent. By contrast, Geelong firm Dennys Lascelles had goodwill of £50 000 on much smaller total assets of £267 000, that is 19 per cent, other smaller firms included Luxmoore Coombs (30%) and Moreheads (31%). For small firms with up to £300 000 total assets, the mean share of goodwill was 20 per cent compared with only 7 per cent for larger companies.

These are smaller social capital shares than produced by the takeover calculations. For most companies, the major balance sheet asset was their loans to farmers, set against the liabilities of paid up capital, loans from banks, and customer deposits. Takeover calculations would merely estimate the net balance between these financial liabilities and assets, and some loans to farmers might not be considered worth their full value. Other balance sheet items were largely physical capital such as property. A case might be made for including loan assets as part of the social capital calculation for the firm. We saw earlier that loans were often made at or below cost in order to draw the farmer into a long term relationship with the agent from which regular marketing commissions would flow. Much depends, however, on whether the loan included a written contractual requirement for the farmer to sell wool through the lending agent. In the absence of an agreement, the loan can be viewed as seeking to draw the farmer into reciprocity and therefore might be viewed as social capital. Such inclusion would have raised the social capital share of most firm's assets to at least 90 per cent. Over time, as the larger firms came to dominate the industry, informal lending practices were transplanted by written contracts.

Conclusion

Our study of stock and station agents in Australian rural communities throws light upon several unresolved issues in the social capital literature. It confirms

empirically the existence of two distinct types of social capital: long term and innate to the nature of a community, and variable in the short term by the planned actions of entities. Indeed, the two types in this case were positively correlated – high innate provided a low cost-high payoff return to planned social capital by creating conducive investment conditions. Further, planned social capital can help to fill the investment shortfall deriving from the public good nature of innate social capital. This was the experience of the agents whose investments helped resolve market failure problems in many struggling rural communities. In the language of development economics, they provided a conduit between top down and bottom up development by combining their linkages into external sources of enterprise with their local social capital investments. Second, we have looked at goodwill as a proxy for measuring the planned social capital investments of firms. While not a perfect match, it provides a worthwhile framework for estimating the size and relative importance of a firm's social capital. The social capital connection to goodwill is a fruitful line of enquiry for future empirical and theoretical research.

Our results intimate the importance of social capital in a formative period of Australian development. Closely-knit but isolated rural communities serving distant and unpredictable commodity markets suggests a climate in which the trust and reputation of social capital would bring major benefits. If social capital is accepted as part of the national accounting framework, this would signify a substantial underestimation of total capital formation and stock in studies of Australian economic development, a process heavily reliant upon the wool staple and the stability of small remote rural communities.³³

Table 1: Social capital as a percentage of takeover price

Bid firm	Target firm	Date	Goodwill value (£000)	Takeover price (£000)	Goodwill as % of price
Goldsbrough Mort	Harrison Jones Devlin	1922	0	169	0
Farmers & Graziers	John Bridge	1919	24	211	11
Dennys LascellesLtd	Dennys Lascelles Austin	1912	50	125	40
Australasian Agency & Bkg	R Goldsbrough	1881	100	232	43
Elders	De Garis	1947	78	165	47
Elders	Hague	1937	76	127	60
Dalgety	Dalgety partnerships	1884	120	180	67
Elders	Wilson, Bolton	1944/5	10	10	100

Sources: Elders N102/319 correspondence, N102/36 Bd meeting; N102/312 balance sheet; Dalgety 2/613/7 prospectus; Goldsbrough Mort 1/12/37 correspondence; *Australasian Insurance & Banking Record*; *Jobson's Investment Digest*; *Wild Cat*.

Table 2: Social capital as a share of total balance sheet assets in the early years of a company or following its acquisition

Agent	Date	Social capital (%)	Total assets (£000)
<u>Large companies</u>			
Elders Smith	1889	1	438
Dalgety	1885	3	3707
Goldsbrough Mort	1889	3	3477
Agency Land & Finance Co Australia	1891	5	572
R. Goldsbrough	1882	6	1571
Farmers&Graziers	1920	7	363
Bennett & Fisher	1920	7	351
Australian Mercantile Loan & Finance	1865	12	611
Harrison Jones Devlin	1892	12	334
Winchcombe Carson	1912	14	301
Unweighted mean		7	
<u>Small companies under £300 000 total assets</u>			
Schute Bell Badgery Lumby	1940	6	216
Webster	1934	10	183
Strachan Murray Shannon	1920	16	157
Dennys Lascelles	1913	19	267
TS Mort	1884	21	241
Pitt Son Badgery	1889	23	129
Younghusband Row	1906	24	190
Luxmoore Coombs	1901	30	66
Moreheads	1921		163
Unweighted mean		20	

Sources: Company balance sheets as produced in various sources including *Australasian Insurance & Banking Record*; *Jobson's Investment Digest*; *Wild Cat*.

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- ¹ I am grateful for comments on an earlier draft by participants at the 2004 combined EHSANZ and AHA conference, also to Leanne Johns, Dr Steve Jones and an anonymous referee.
- ² For a history of the industry see Simon Ville, *The Rural Entrepreneurs. A History of the Stock and Station Agent Industry in Australia and New Zealand* (Melbourne, 2000).
- ³ There have been many contributions to a conceptual understanding of social capital. Pierre Bourdieu, 'The Forms of Capital' in J. G. Richardson ed. *Handbook of Theory and Research for the Sociology of Education* (New York, 1986); James S. Coleman, (1988) 'Social Capital in the Creation of Human Capital', *American Journal of Sociology* Supplement XCIV (1988), 95-120; Robert D. Putnam, *Bowling Alone. The Collapse and Revival of American Community*. New York, 2000); Joel Sobel, 'Can We Trust Social Capital?' *Journal of Economic Literature* 40 (2002), 139; Francis Fukuyama, *Trust: the Social Virtues and the Creation of Prosperity* (New York, 1995). Edward L. Glaeser, David Laibson, Bruce Sacerdote, 'An Economic Approach to Social Capital', *Economic Journal* CXII (2002); Alejandro Portes, 'The Two Meanings of Social Capital', *Sociological Forum*, XV (2000), 3-4; Christian Grootaert, 'Social Capital: the Missing Link?', *Social Capital Initiative Working Paper* no. 3 (1998), 8. Samuel Bowles and Herbert Gintis, 'Social Capital and Community Governance', *Economic Journal* 112 (2002); Michael Woolcock, 'Social Capital and Economic Development: Towards a Theoretical Synthesis and Policy Framework', *Theory & Society* 27 (1998); Tom Schuller, Stephen Baron, and John Field, 'Social Capital: a Review and Critique' in Stephen Baron, John Field, and Tom Schuller eds *Social Capital. Critical Perspectives* (Oxford, 2000); Shelagh Ogilvie, *A Bitter Living - Women, Markets, and Social Capital in Early Modern Germany* (Oxford, 2003).
- ⁴ Putnam, *Bowling Alone*; Susan Keen, 'Associations in Australian History: Their Contribution to Social Capital', *Journal of Interdisciplinary History* 29, (1999).
- ⁵ Jack P. Greene, 'Social and Cultural Capital in Colonial British America: a Case Study' in Robert I. Rotberg ed. *Patterns of Social Capital. Stability and Change in historical Perspective* (Cambridge, 2001); B. Zorina Khan, 'Order with Law: Social Capital, Civil Litigation and Economic Development', *Australian Economic History Review* 39 (1999); M. D. R. Evans, 'Participation in Voluntary Organizations, Australia 2001-2', *Australian Social Monitor* 6 (2003); Jenny Onyx and Paul Bullen, 'Measuring Social Capital in Five Communities', *Journal of Applied Behavioral Science* 36, (2000); For methodology of measurement also see Colin J. Macgregor, and John Cary, 'Social/Human Capital

Rapid Appraisal Model (SCRAM): a Method of Remotely Assessing Social and Human Capacity in Australian Rural Communities', *Rural Society* 12 (2002), 109; A. Black and P. Hughes, *The Identification and Analysis of Indicators of Community Strength and Outcomes* (Canberra, 2001).

⁶ Onyx and Bullen, 'Measuring'; Evans, 'Participation'; Coleman, 'Social capital'; Glaeser et al, 'Economic approach', 439.

⁷ Marjorie K. McIntosh, 'The Diversity of Social Capital in English communities, 1300-1640 (With a Glance at Modern Nigeria)' in Rotberg, ed. *Patterns*; Claudia Goldin and Lawrence F. Katz, 'Human Capital and Social Capital. The Rise of Secondary Schooling in America, 1910-40' in Rotberg, ed. *Patterns*; Stephen Knack and Philip Keefer, 'Does Social Capital Have an Economic Payoff? A Cross-Country Investigation', *Quarterly Journal of Economics* 112 (1997) c. 11 concluded that levels of trust tend to be higher in ethnically homogeneous communities following non-hierarchical religions particularly Protestantism. G. F. James, ed. *A Homestead History. The Reminiscences and Letters of Alfred Joyce of Plaistow and Norwood, Port Phillip, 1843-64* (Melbourne, 1949), 63; Stephen Henry Roberts, *The Squatting Age in Australia, 1835-47* (Melbourne, 1935), 368-75.

⁸ Rod Lancashire, 'European-Chinese Economic Interaction in a pre-Federation Rural Australian Setting', *Rural Society* 10 (2000), 229, 237-8; James Logan, 'Sectarianism in Ganmain: a Local Study, 1912-21', *Rural Society* 10 (2000), 121. Also see Keith Swan, *A History of Wagga Wagga*. Wagga (Wagga, 1970); Hugh R. Jackson, *Churches and People in Australia and New Zealand, 1860-1930* (Wellington, 1987); Malcolm Campbell, *The Kingdom of the Ryans* (Sydney, 1997).

⁹ Geoff Raby, *Making Rural Australia. An Economic History of Technical and Institutional Creativity, 1788-1860* (1996), ch. 6. Keen, 'Associations', c.13. Ros Derrett, 'Festivals and Regional Destinations: How Festivals Demonstrate a Sense of Community and Place', *Rural Society* 13 (2003).

¹⁰ Noel Butlin Archives Centre, Australian National University Canberra (hereafter NBAC), Dalgety Collection Edmund Doxat, Chairman of Dalgety. N8/24. James ed. *Homestead*, 62, 64-5, 106-8.

¹¹ Noel G. Butlin, *Forming a Colonial Economy*, (Cambridge, 1994), 181, 185, 195. Graeme J. Abbott, *The Pastoral Age: a Re-examination*, (Melbourne, 1971), 118-24; Sharon Morgan, *Land Settlement in Early Tasmania*, (Cambridge, 1992), 57-64; Dawn May, *Aboriginal Labour and the Cattle Industry: Queensland from White Settlement to the Present*, (Cambridge, 1994), 29-38. Alan Barnard, *The Australian Wool Market, 1840-1900*, (Melbourne, 1958).

¹² Khan, 'Order'.

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- ¹³ NBAC, Dalgety, N8/20, F. G. Dalgety Letterbook, 1852-4; S. Ville and G. Fleming, 'From kinship to relations economic? The development of pastoral networks in Australasia'. In Anthony Slaven and Michael Moss (eds) *Entrepreneurial Networks and Business Culture* (Madrid, 1998), 115-33.
- ¹⁴ Bourdieu, 'Forms', 249-50. Glaeser et al, 'Economic Approach', 443.
- ¹⁵ NBAC, AMLF 97/36/30/2; 97/36/16/1; Dalgety N8/24 letters 1887; AMLF 97/36/41/1, letters 1924.
- ¹⁶ Glaeser et al, 'Economic approach', 442; NBAC Elders N102/25 in 1923 and N102/30 in 1936.
- ¹⁷ NBAC, Elders N102/38. Board memoranda 1950. Winchcombe Carson K8189 correspondence 193; Webster, *Century Of Service*, 13. James *Homestead*, 112. Wild Cat 4/6/27, 248; Elders N102/97, letters 1908.
- ¹⁸ Craig Muldrew, *The Economy of Obligation: the Culture of Credit and Social Relations in Early Modern England* (Basingstoke, 1998).
- ¹⁹ 'Strachan and Co. Limited' *Wool's Statistical Service* 26.8.1935; James, *Homestead*, 113-15. A Dalgety report in 1936 emphasised the value of cars in 'retaining old and securing new connections'. NBAC, 100/1/30/33, branch reports. Ville, *Rural Entrepreneurs*, 161-2.
- ²⁰ Data from *Dalgety's Annual Wool Review*, *Australasian Insurance and Banking Record*, and *Australian Pastoralists Review* for various years.
- ²¹ Ville, *Rural Entrepreneurs*, 94.
- ²² NBAC, Winchcombe Carson K8189, correspondence.
- ²³ NBAC, Elders N102/97, correspondence, 1908. Agricultural societies were being superseded by publicly funded government research stations and agricultural extension. Dirk H. R. 'Science and Education: the Beginnings of Agricultural Extension in 1890s New South Wales', *Rural Society* 10, (2000).
- ²⁴ NBAC, Dalgety 100/1/35/20. Managers report 30 June 1942. Dalgety 163/27. Managers conference 1960. Elders 103/4. Post-World War Two review.
- ²⁵ Experimental methods, increasingly popular in economics, are viewed as a way of overcoming participant bias. Rather than ask opinions, experimental methods seek to elicit a sincere response by working through a laboratory scenario that mimics a contemporary real world reaction by the participant.
- ²⁶ Putnam, *Bowling alone*; Knack and Keefer, 'Does social capital have an economic payoff?' pp. 9-10 distinguish 10 different types of formal association. Also see Fukuyama's attempt to distil differences

of organisational cohesion and trust into a single formula. Francis Fukuyama, 'Social Capital and Civil Society', IMF conference on Second Generation Reforms, (1999), 6-9.

²⁷ Black & Hughes, *Identification and Analysis*.

²⁸ NBAC, Goldsbrough Mort 2A/30/35, correspondence. Elders N102/312

²⁹ Kenneth Arrow, 'Observations on social capital'. In P. Dasgupta & I. Serageldin eds *Social Capital: A Multifaceted Perspective* (Washington DC, 1999). Sobel, 'Can We Trust', 144-5. N102/312. 100/7/116. *Australian Investment Digest* 1.5.1923, 70; Steven Tadelis, 'What's in a name? Reputation as a tradeable asset' *The American Economic Review* LXXXIX (1999), 548-63. Also see David M. Kreps, 'Corporate culture and economic theory'. In James E. Alt and Kenneth A. Shelpse eds *Perspectives on Positive Political Economy* (New York, 1990), 90-143.

³⁰ NBAC, Elders N102/312; Goldsbrough Mort 100/7/116. *Australian Investment Digest* 1.5.1923, 70.

³¹ In many cases employees of the acquired company had to sign an oath not to conduct a stock and station agency business for five years or so.

³² Annual Report 1888.

³³ Noel G. Butlin, 'Australian national accounts'. In Wray Vamplew ed. *Australians. Historical Statistics* (Broadway, NSW, 1987).