Trust, Finance, and the Intangible Economy*

Dan Su[†] Rusi Yan[‡]

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Abstract

We emphasize the significant social and financial hurdles in a country's transition to an intangible economy. Our findings reveal a strong correlation between a country's *social trust*, its *economic structure*—reflected by the proportion of intangible-intensive sectors—and its *financial structure*, marked by the prevalence of cash-flow-based over asset-based lending. This relationship is explained through a two-sector growth model with endogenous economic and financial structures, where trust affects the difficulty of borrowing without collateral. Our model identifies multiple steady states and illustrates that in a high-trust equilibrium, the feedback loop between the development of earnings-based lending technology and the growth of the intangible-intensive sector significantly boosts aggregate productivity. Lastly, our quantitative analysis underscores the crucial role of social trust in explaining cross-country differences in productivity and intangible capital via the *type* of financial friction channel.

JEL codes: D53; G20; O11; O16; O17; Z13

Keywords: trust; type of borrowing constraint; structural change; intangible capital

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[†]Department of Finance, Cheung Kong Graduate School of Business. Email address: dansu@ckgsb.edu.cn

[‡]School of Finance, Central University of Finance and Economics. Email address: rusi.yan@cufe.edu.cn