The Economics of Reputational Information

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Reputational Information

- Reputational information = information about an actor’s past performance that helps a decision-maker predict the actor’s future performance

- Examples:

<table>
<thead>
<tr>
<th>Unmediated</th>
<th>Mediated</th>
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<tbody>
<tr>
<td>• Word of mouth</td>
<td>• Credit scores</td>
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<td>• Recommendation letters and references</td>
<td>• Investment ratings (bonds, mutual funds)</td>
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<td>• Job evaluations and student evaluations</td>
<td>• GPAs</td>
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<td>• Consumer product reviews and ratings (Amazon star ratings; Ratemyprofessor.com; Avvo; Ripoff Report; BBB)</td>
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<td>• Voting systems? PageRank, Digg</td>
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Undersupply Concern

- The market’s invisible hand is predicated on consumers rewarding good producers and punishing poor ones
  - Reputational information = invisible hand of the invisible hand
- Concern: every consumer has private information about their marketplace experiences
  - Costs: time, vendor retribution, norms against public criticism, privacy, legal risks
  - Benefits: usually only psychic rewards (pulls towards love it or hate it)
- But consumers communicate that private information into the marketplace through their decisions
- But...
  - Most marketplace decisions are private information
  - Most aggregations of marketplace behavior aren’t readily available
- Possible solutions
  - Reduce legal disincentives for consumers to share their marketplace experiences
  - Make consumer marketplace decisions public information
  - Government funding of reputational information production