

CHAPTER 1

GENERAL INTRODUCTION

1.1 Background

Trust and risk concepts are widely used to explain interpersonal relationships in many social science disciplines such as economics, psychology, philosophy and management studies (Sodano, 2002). However, there are no enough empirical literatures available that examine the impact of trust on risk attitude of rural people particularly in Ethiopia. Our study in general focuses on this knowledge gap to provide empirical evidence that shows the role of trust in risk attitude of the Ethiopian households. To carry out the empirical study, availability of quality data and the methods for quality control are some of the basic issues that should be inspected very well to reach at the final conclusion (Anderson & Mellor, 2009; Dohmen et al., 2011). But first, it is important to explain the concepts and theoretical framework of the trust and risk attitude comprehensively (Harbaugh, Krause, & Vesterlund, 2002). Schlottmann & Anderson (1994) discussed in their study about the importance of diverse information sources and sufficient sample data to reach a conclusion and recommendation. A research conducted by Picazo-Tadeo & Wall (2011) states that countries which do not pay close attention to trust and risk behaviors of their people usually fall behind in pursuing inclusive-development¹. This affects particularly the mutual relationship between the producers and government institutions that eventually and consequently lead to undermining the decision-making abilities of the individuals in activities and investments that have considerable impact on economic and social growth of the people. For example, Fukuyama (1995) says Japan, Germany and the United States are ‘countries of rich and complex civil societies’ and their development stems from the high-trust family activities and society rules. Individuals’ role and their relationship with their community embody trust that helps them reduce social barriers and uneasiness among the people for productive interactions (Fox, 1974). Institutions as well intend to develop rules and regulations based on trust and trustworthiness to improve social cohesion and harmony within communities (Farrell & Knight, 2003). Hence lack of institutional approach to

trust and risk attitudes of individuals in a society have unintended consequences for the overall development of a country.

Ethiopia, a nation once named as a least developed country, now seems to change its gloomy past by promoting small scale farming at grass-root levels. In 2003, African countries promised to allocate 10% of their annual budget on agriculture at the African Union Summit (Maputo Declaration). The statistical data of the annual report of IFPRI's Regional Strategic Analysis and Knowledge Support System (ReSAKSS) shows that seven African countries hit the target in most years. Ethiopia, among the seven countries maintained the pledge of focusing on the strategies and ways of reaching out small-scale farming households in order to learn their socio-economic situations and improve their productivity to reduce poverty and eliminate hunger through agriculture (Benin & Yu, 2012). However, further researches have been initiated afterwards to understand the basic needs of the farmers and their risk attitude on technology adoption (E.g. fertilizer-seed choice). The cultural and traditional lives of the Ethiopian people have evolved under different circumstances and as a consequence they have different forms of socio-economic virtue and behavioral reactions toward the natural risk phenomenon. Some empirical studies suggest, that many of rural people are highly influenced by the amounts of risks they face. For example, farmers in developing countries are reluctant to use fertilizers, irrigation technology and other agricultural inputs that have profitable returns and the reason is their risk averse attitude toward the adoption (Yesuf & Bluffstone, 2008).

Many studies provide evidence for the presence of strong risk aversion attitude in developing societies. In 2008, Yesuf and Bluffstone conducted an experimental study on the risk aversion behavior of the Ethiopian households in the area where severe shocks such as erratic rainfall, higher rates of livestock mortality are common. The study reports that more than half of the households exhibit extreme risk aversion attitude. Gender of the household, age, literacy, dependency ratio², values of the domestic animals are some of the significant variables that affect the risk aversion attitude of the households. Similarly, Asian household decision makers having similar development

² Dependence ration refers to the ratio of number of household members below age15 to above age 15.

levels demonstrate moderate risk aversion behavior. Likewise, another research was conducted in the northern highlands of Ethiopia in a village called Abraha We Atsbeha, an area where poverty is highly prevalent. The study finds a strong risk aversion attitude among the Ethiopian farmers. Both studies took place in the regions where extreme shocks are widely experienced in addition to population pressure, poor arable land and erratic rain fall (Akay, Martinsson, Medhin, & Trautmann, 2012). Our study is carried out in the southern part of Ethiopia where the aforementioned shocks are rarely to occur relative to the other regions of Ethiopia. The area has different socio-cultural and geographic features; generally flat landscape compared to the northern part where the terrain is very rugged.

1.2 Knowledge Gap

Several studies have been conducted to investigate and assess the risk attitude of rural households. The major objective of the studies is to establish a comprehensive scientific literature that explains the connection between the risk attitude and the determining factors that affect it at the household level. Several kinds of human characteristics may be involved to shape attitudes that eventually transform to behaviors and finally to culture. Hence, studying and investigating what factors determine the attitudes of people are necessary to formulate new policies and instruments that suit those attitudes and behaviors in focus for positive outcome. Many studies come up with a conclusion that the attitudes of individuals are more or less linked to their economic background and decision-making abilities when they are faced with uncertain situations (Dohmen et al., 2011). Nevertheless, households often face risky situations from other dimensions of life as well, be it socially, environmentally or politically. Agricultural production, seasonal rainfall variations, shocks from drought and flooding, lack of market information are some of the most common risky situations that frequently keeps farmers in dilemma. As a result, a number of studies are conducted to compute and understand their influences on the attitudes of the households. Previously a risk preference analysis was carried out in the northern part of Ethiopia, a region where ethnographically belongs mostly to the Tigryans and Amharas. The area is ecologically prone to drought and erratic rainfall unlike the southern regions with relatively stable household income and the areas are noted for their verdant evergreen forests (Amare,

1987). The studies find out that most of the farmers are risk averse. The determining factors of the risk attitude include personal and socio-economic characteristics of the households (Akay et al., 2012). However, even though the studies capture most of the variables for the analysis, the importance of certain societal norms and technological assets in the Ethiopian society are not discussed in the literatures (E.g. trust). Trust as an explanatory variable and influential trait is assumed to have significant effect on the risk attitudes of rural people. Hence our study sees the importance of trust among the Ethiopian society and we include it in the analysis to test its significance as a determining factor in risk attitude. In addition, the expansion of new technology such as mobile phone usage by the rural people is regarded as the most effective communication tool to connect the sellers and buyers as well as for sharing information within the communities. Consequently, mobile phone ownership is also included as an independent variable to measure the effect on the risk preference of the subjects. Furthermore our study establishes a link between the risk attitude and the ‘trust in relatives’ of the subjects to define the relationships between them and to explain what it means to the households. To fill the knowledge gap, our study points out the main objectives and the necessary research questions that lead to the focused discussion, conclusion and policy recommendations.

1.3 Research Objectives

The main objective of the study is to investigate the risk attitude of the Ethiopian households in the southern region and the factors that affect the individuals’ attitude. It is intended to capture the potential influencing factors that contribute to the development of the risk attitude of the Ethiopian households.

Moreover the study shows the relationship between the risk-seeking individuals and the trust in their relatives and its influence on other independent variables. Previous literatures conferred the importance of trust on risk preference but an empirical analysis is crucial to measure the influence.

1.4 Research Questions

This study seeks answering the following research questions:

1. What are the main determining factors of the Ethiopian households' risk preference attitude?
2. Is the risk-seeking attitude common among the Ethiopian households?
3. How do gender and education affect the risk-taking behaviors of the interviewed households in Ethiopian?
4. Does communication technology such as mobile phones encourage households to take more risks in farm management?
5. Does a survey data can predict the actual risk-taking attitude of the subjects in the lottery game?
6. What is the implication of the risk results on the policy formulation for the Ethiopian people based on the data collected from the study area?
7. Why risk attitude assessment is important to the Ethiopian households and what is its contribution to their welfare?

1.5 Outline

The thesis is divided into seven chapters. After this introductory chapter, the literature review follows with detailed descriptions of risk to shed light on the previous studies and findings of the risk attitude that have been carried out in different regions of the world, particularly in Ethiopia. The literature review is also divided into sub-sections to discuss the risk concepts, risk aversion and risk loving attitude of individuals and finally completing the section with the explanation of trust and social capitals and their effect across different spectrums of social life of individuals. Each of the sub-topics compares the differences and similarities among the many different study reports. Chapter three discusses the conceptual framework of risk attitude. It illustrates a graphical representation of the process where attitude is influenced by the socio-economic and political variables to provide the basis for model specifications. The next chapter explains the methodology that we have followed to collect our data. It details the study area, the independent variables, their measurements as well as the causal

assumptions and influences on the risk attitude. It talks about the models that we employ to run the regression. Both Probit and Ordinary Least Square (OLS) models are chosen to explain the relationships between the independent and dependent variables. Chapter five interprets the results of the regression models and compares it with different study results. It contains two main sub-sections: survey-based results and the results obtained using the lottery game. The last section presents the conclusions drawn from out the study and some of the policy recommendations to improve the risk-taking attitude of the Ethiopian households.



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