OPPORTUNITIES AND RISKS OF TRANSPARENCY IN MARKETS

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ABSTRACT

Transparency, the disclosure and sharing of an abundance of information, has been championed as a more desired quality of business markets over the last decade, particularly in connection with financial markets, electronic business exchanges, supply chain management, and buyer-seller relationships. Recent attention given to transparency has been driven by advances in information technology, globalization of business, financial events, rising norms for disclosure and data exchange standards, and the development of closer supply, distribution, and customer relationships. The article focuses on transparency at market and business relationship levels, where there is public, market, or, at least, relationship disclosure of information about prices, costs, volume, suppliers, buyers, subsequent customers, and product and service features.

An abundance of shared information is predicted to lead to markets and business relationships that are characterized by transparent prices and increasingly transparent product and participant features. A substantial increase in the transparency of markets may well lead to substantial changes in the conditions of markets and to vigorous competition, conditions that may be legitimately resisted by suppliers and buyers. The authors' discussion of transparency is grounded in theory of perfect markets, transaction costs, and principal-agent relationships. Promises and realities of electronic markets, at least as suggested in early research, are used to examine potential benefits and costs of transparency.

For example, in a perfect market with product homogeneity, perfect transparency, and accurate information interpretation, competitive price comparisons by buyers and suppliers could produce high elasticity, quick price responses, and lower prices (Smith, Bailey, and Brynjolfsson 2000). Transparency of supply and inventory holding could result in cost savings from inventory control that offset the effects of lower prices on profitability. Predicted risks of open markets include price volatility and erosion of margins, but early research of electronic markets characterized by price and supply visibility has not consistently shown price volatility or that prices have been driven to marginal cost levels. Price competition may be softened by the buyer's increased ability to search for differentiated products or by the suppliers' increased ability to signal differentiation through transparency of product features and quality.

Transparency, as facilitated by technology, also provides opportunities for reductions in opportunism, uncertainty, and costs of searching for, acquiring, and processing information by both buyers and suppliers (Kulkarni 2000). Transparency may reduce ex-ante uncertainty in forming relationships and, thus, reduce transaction costs associated with contracting, monitoring, and enforcing agreements (Picot, Bortenlanger, and Rohrl 1997). Evidence from electronic markets suggests that, while search costs are reduced, high levels of uncertainty and dynamism remain, perhaps due to an increase in ex-post uncertainty. The exchange of information may facilitate a rapid modification of products, prices, and other elements of relationships, necessitating renegotiation among partners. Further risks of transparency are information overload, associated communication failures and maladaption costs.

The authors identify other opportunities and risks associated with transparency of markets and buyer-seller relationships, such as the potential for collusion (Foer 2001), the loss or gain of informational advantages, and enhancement of planning and product development. At the risk of losing informational advantage in a relationship, partners willing to share proprietary information with each other may gain competitive advantages through enhanced communications and trust that are facilitated by transparency (Kulkarni 2000). However, the relationship between the degree of transparency and the benefits derived from the same may be curvilinear, suggesting that perfect transparency is not optimal for markets or for buyer-seller relationships.

References and the full paper are available from the authors.