

Buying Reputation as a Signal of Quality: Evidence from an Online Marketplace*

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Abstract

Seller reputation, generated by buyer feedback, is critical to fostering trust in online marketplaces. Marketplaces or sellers may choose to compensate buyers for providing feedback. Signaling theory predicts that only sellers of high-quality products will reward buyers for truthful feedback, especially when a product lacks any feedback and when the seller is not established. We confirm these hypotheses using Taobao's "reward-for-feedback" mechanism. High-quality products, especially without established feedback, are chosen for feedback rewards, which cause sales to increase by 36%. Marketplaces and consumers can therefore benefit from allowing sellers to buy feedback and signal their high-quality products in the process. *JEL* Classifications: D47, D82, L15, L86.

Keywords: reputation, feedback, ratings, signaling, rebate mechanism, Taobao.

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