

The costs and benefits of social ties

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Socializing an undersocialized field

- In a much-cited (45,000+) article, Mark sociologist Granovetter bemoaned the ‘oversocialization’ of his own field, and contrasted it with the ‘undersocialization’ of neoclassical economics
- He proposed a compromise of sorts – social relations were not destiny, but they were the essential structure within which economic relations exist
- In Granovetter’s proposed middle ground, economic exchange is “embedded” in a set of social relations
- Implicit in this formulation is the need to account for the interaction of social and economic forces in determining behaviors

Social relations and economic action

- In this presentation, I will focus on a set of 'economic actions' that are affected by actors' social relations.
- The consequences of social relations is a set of tradeoffs, most prominently (for our purposes here):
 - Reduced information frictions (both ex ante and ex post)
 - Favoritism
- Why we care: These forces may affect (among other things), the allocation of physical and human capital

Examining the effects of social ties

- We may consider two related questions:
 - How much do social ties affect allocation decisions? (i.e., is there a quantity effect)
 - Do social ties improve or worsen the quality of allocation decisions?
- There is no single answer! In a given context, it depends on the strength of the just-noted counteracting effects, as well as distinct features of the setting (e.g., strategic and/or enforcement efforts). As a result (in the spirit of the embeddedness critique!), these are *setting-specific* empirical questions

Goals of the presentation

- Emphasize that – very plausibly – social ties have potentially positive and negative consequences *even in the same broad institutional setting*
- Provide a sense of common methodologies deployed to identify the role of social ties, and why we might care about each of these findings

Some methodological themes

- Measurement
- Identification

Measurement

- Social ties

- Naturally, the source of social connection varies across settings
- We are generally limited to studying readily observable social ties, which may have different implications from unobserved ones

- Outcomes

- It will be useful (in terms of motivating question) to consider contexts in which there is an outcome associated with a plausible social welfare ranking
- This will allow us to consider whether social ties improve individual versus societal outcomes

Identification – non-randomness of ties

- If individuals and/or organizations exploit social ties for individual or group benefit, assignment cannot be random
- Implication I: Often, the empirical approaches we employ are imperfect, e.g., exploit discrete changes around turnover and/or events that “shock” the value of social ties
- Implication II: This leads to fixed-effects panel estimates that may understate the ‘true’ costs and benefits of social networks (which may be present in part in hard-to-interpret cross-sectional variation)

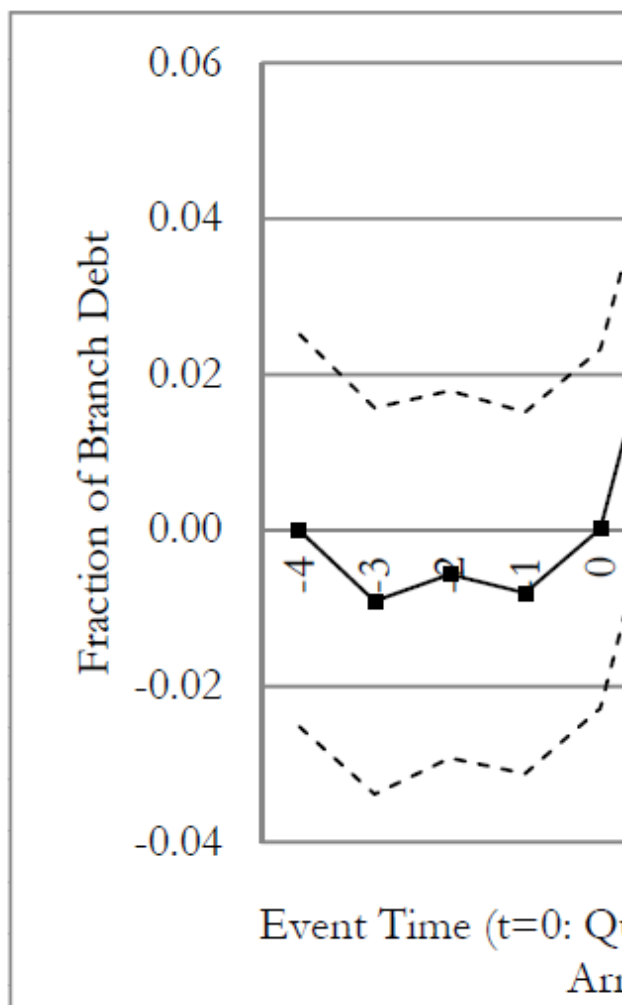
Work cited in this presentation

- Fisman, Raymond, Daniel Paravisini, and Vikrant Vig. "Cultural proximity and loan outcomes." *American Economic Review* 107.2 (2017): 457-92.
- Fisman, Raymond, et al. "Experience of communal conflicts and intergroup lending." *Journal of Political Economy* 128.9 (2020): 3346-3375.
- Fisman, Raymond, et al. "Social ties and favoritism in Chinese science." *Journal of Political Economy* 126.3 (2018): 1134-1171.
- Chu, Jian, et al. "Hometown Ties and the Quality of Government Monitoring: Evidence from Rotation of Chinese Auditors." *American Economic Journal: Applied Economics* 13.3 (2021): 176-201.
- Fisman, Raymond, et al. "Social ties and the selection of China's political elite." *American Economic Review* 110.6 (2020): 1752-81.

Setting 1 – Indian credit markets

- Social ties
 - Religion and (for Hindus) caste affiliation, as documented by bank records and/or name matching
- Outcomes
 - Credit allocation, which has a clear link to allocative efficiency based on credit default
- Identification
 - Bank loan officers are *not* randomly assigned (nor would we say that they should be!) but they experience frequent rotations
 - Plausibly assignment is random conditional on a ‘saturated’ set of controls

Social ties and credit allocation - quantity



Credit allocation to borrowers from *incoming* branch manager's group



Credit allocation to borrowers from *outgoing* branch manager's group

Social ties and credit allocation - quality

Dependent Variable	Ex-Post Loan Quality	
	Fraction of Borrowers	
	In Default in $t+4$	
	(1)	(2)
SameGroup	-0.0060** (0.003)	
SameGroup \times SameGroup $_{t+4}$		-0.0082* (0.005)
SameGroup \times (1- SameGroup $_{t+4}$)		-0.0137*** (0.005)
Branch-Group Fixed Effects	Yes	Yes
Branch-Quarter Dummies	Yes	Yes
Group-District-Quarter Dummies	Yes	Yes
Observations	98,229	81,482
R-squared	0.814	0.515

Source: Fisman, Paravisini, and Vig (2017)

Cultural proximity and lending – summary

- Cultural closeness increases the *quantity* of credit
 - This is consistent with both favoritism and reduced information frictions (ex ante and/or ex post)
- Cultural closeness increases the *quality* of credit
 - This suggests that, at least in a static environment, cultural closeness improves allocative efficiency
 - Many caveats – leads to greater social segmentation, and may even give rise (as in Coate-Loury) to minority discrimination

Cultural proximity and lending – summary

- These findings *do not* imply an absence of favoritism, merely that they are dominated in this case by reduced information frictions
- In a follow-up paper we consider a *shock* to favoritism to potentially isolate this consequence of social ties

Intergroup frictions and economic outcomes

- This follow-up paper attempts to answer a distinct (but related) question: the formation and persistence of out-group animosity or in-group favoritism
- This focus is of particular relevance given theory and cross-sectional evidence on ethnic divisions and economic outcomes (e.g., Easterly and Levine, 1997)

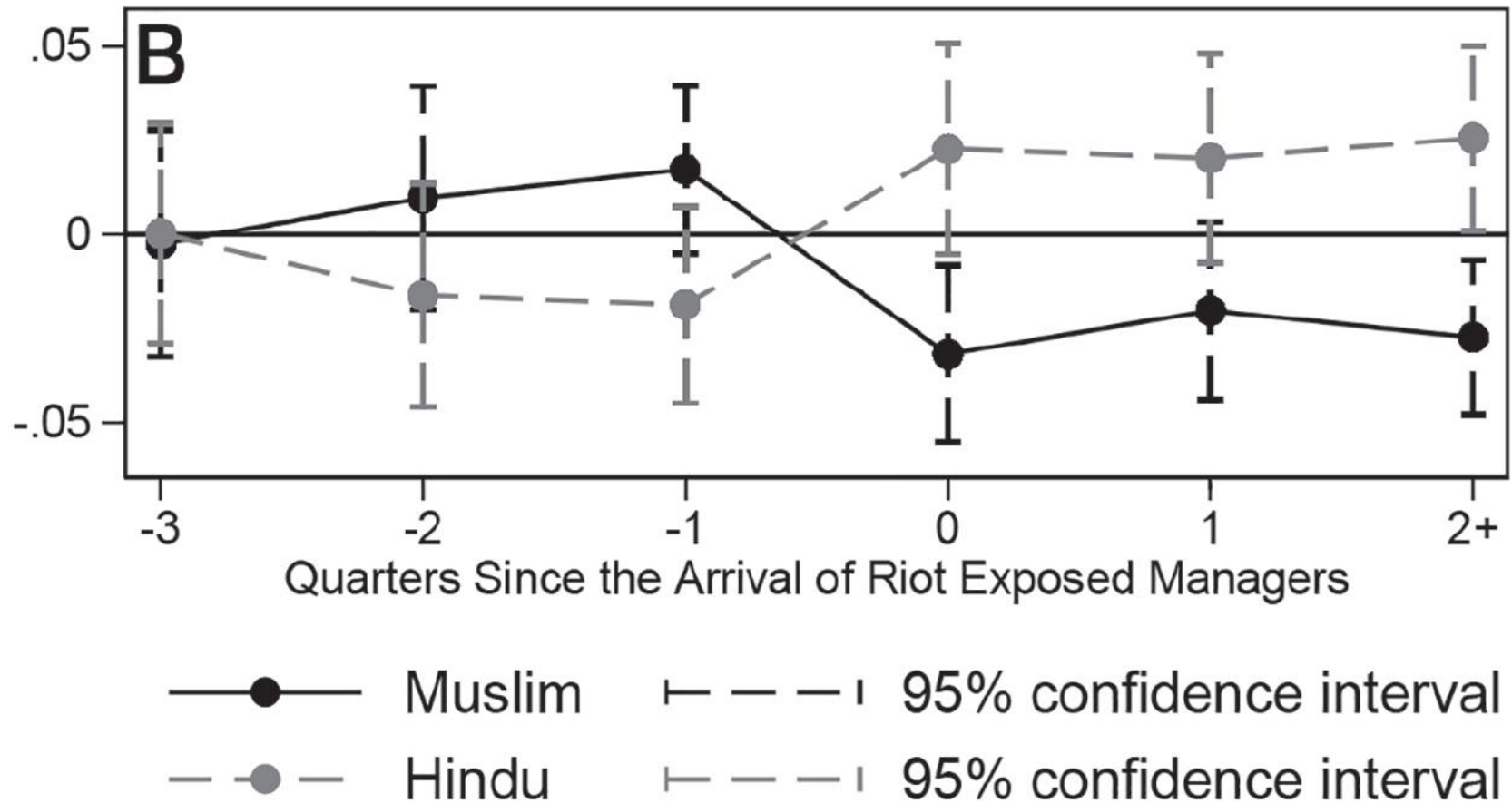
Setting 2: Riots and Lending

- We focus in on *Hindu* branch managers (the substantial majority of cases), using variation in exposure to religious violence
- This captures the *change* in favoritism in a panel setting

Less lending to Muslim borrowers

	NEW DEBT/ \sum NEW DEBT			NO. NEW LOANS/ \sum NO. NEW LOANS		
	Muslim Borrowers (1)	Hindu Borrowers (2)	Other Borrowers (3)	Muslim Borrowers (4)	Hindu Borrowers (5)	Other Borrowers (6)
RiotExperience dummy	-.043*** (.013)	.040*** (.014)	-.011 (.013)	-.029*** (.010)	.028** (.012)	-.007 (.012)
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Branch	Yes	Yes	Yes	Yes	Yes	Yes
District \times time	Yes	Yes	Yes	Yes	Yes	Yes
Home district \times time	Yes	Yes	Yes	Yes	Yes	Yes
R^2	.729	.746	.777	.812	.796	.794
Observations	11,799	12,594	9,095	11,799	12,594	9,095

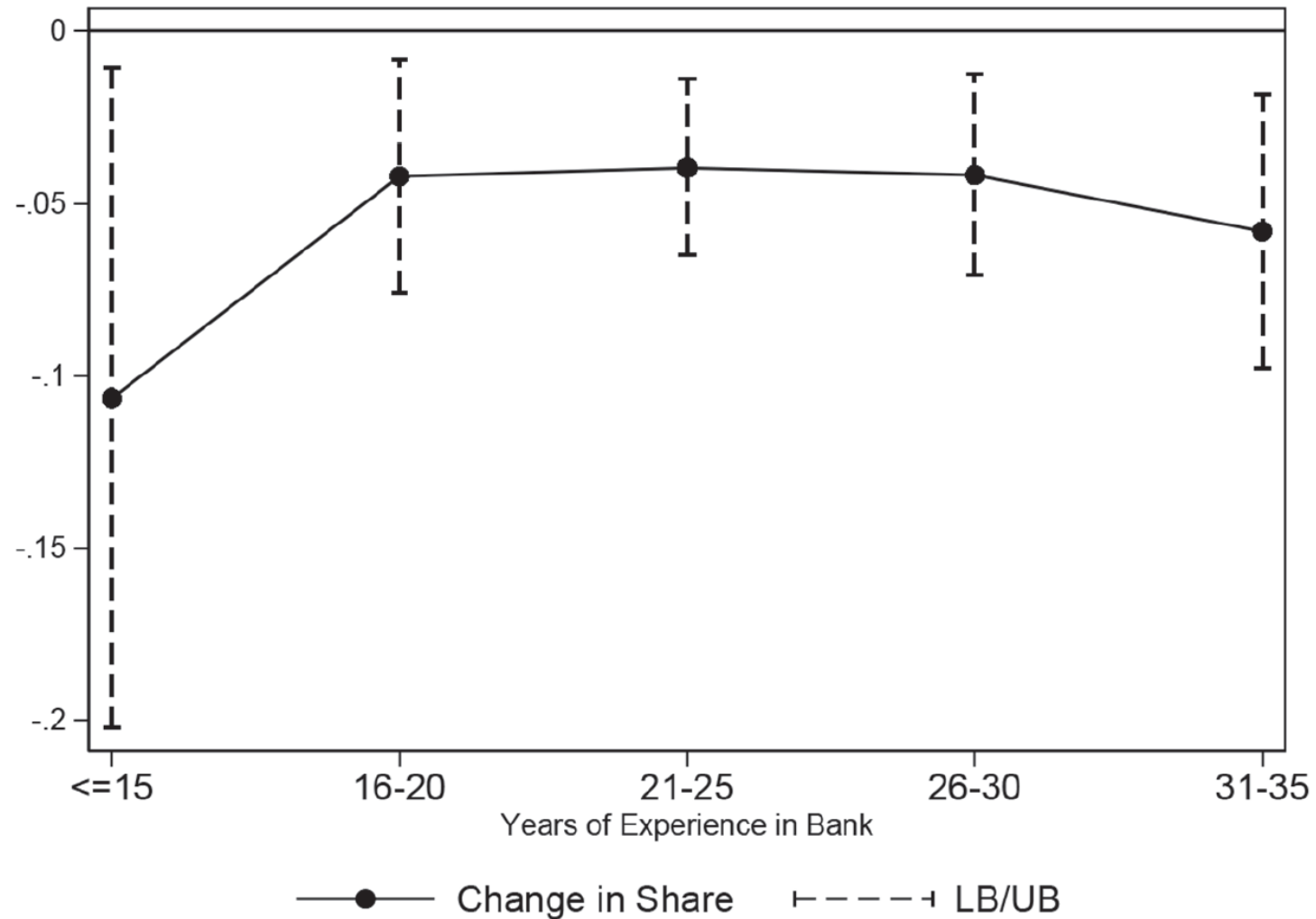
Less lending to Muslim borrowers



Lower probability of Muslim default

	DEFAULT ON LOANS EXTENDED			
	(1)	(2)	(3)	(4)
Riot	-.023*** (.011)	-.023*** (.011)	-.036*** (.018)	-.035*** (.018)
Non-Muslim borrowers × Riot	.023*** (.011)		.025*** (.012)	
Hindu borrowers × Riot		.023*** (.011)		.025*** (.012)
Other borrowers × Riot		.023 (.020)		.025 (.020)
Controls	Yes	Yes	Yes	Yes
Branch × religion	Yes	Yes	Yes	Yes
District × religion × time	Yes	Yes	Yes	Yes
Home district × time	No	No	Yes	Yes
R^2	.494	.494	.608	.608
Observations	25,334	25,334	24,534	24,534

The effects are persistent



Intergroup frictions and lending – summary

- Aggravating intergroup animosities can lead to long-lasting *economic* divisions, with negative social welfare consequences
- This does not capture the sum total consequences of intergroup animosities – which on average are canceled out by efficiency benefits from reduced frictions

Setting 2 – Chinese scientific research

Setting 2 – Chinese scientific research

- Social ties
 - Follow earlier literature in emphasizing hometown, college, and workplace overlap.
 - We will see why this might matter (as distinct from directly observing who is dining with whom, etc)
- Outcomes
 - Quality of scientific research (e.g., citations, H-Index)
- Identification
 - Rotation onto (and off) selection committee for Chinese Academy of Sciences
 - (Plausible placebo in presence of non-committee members)

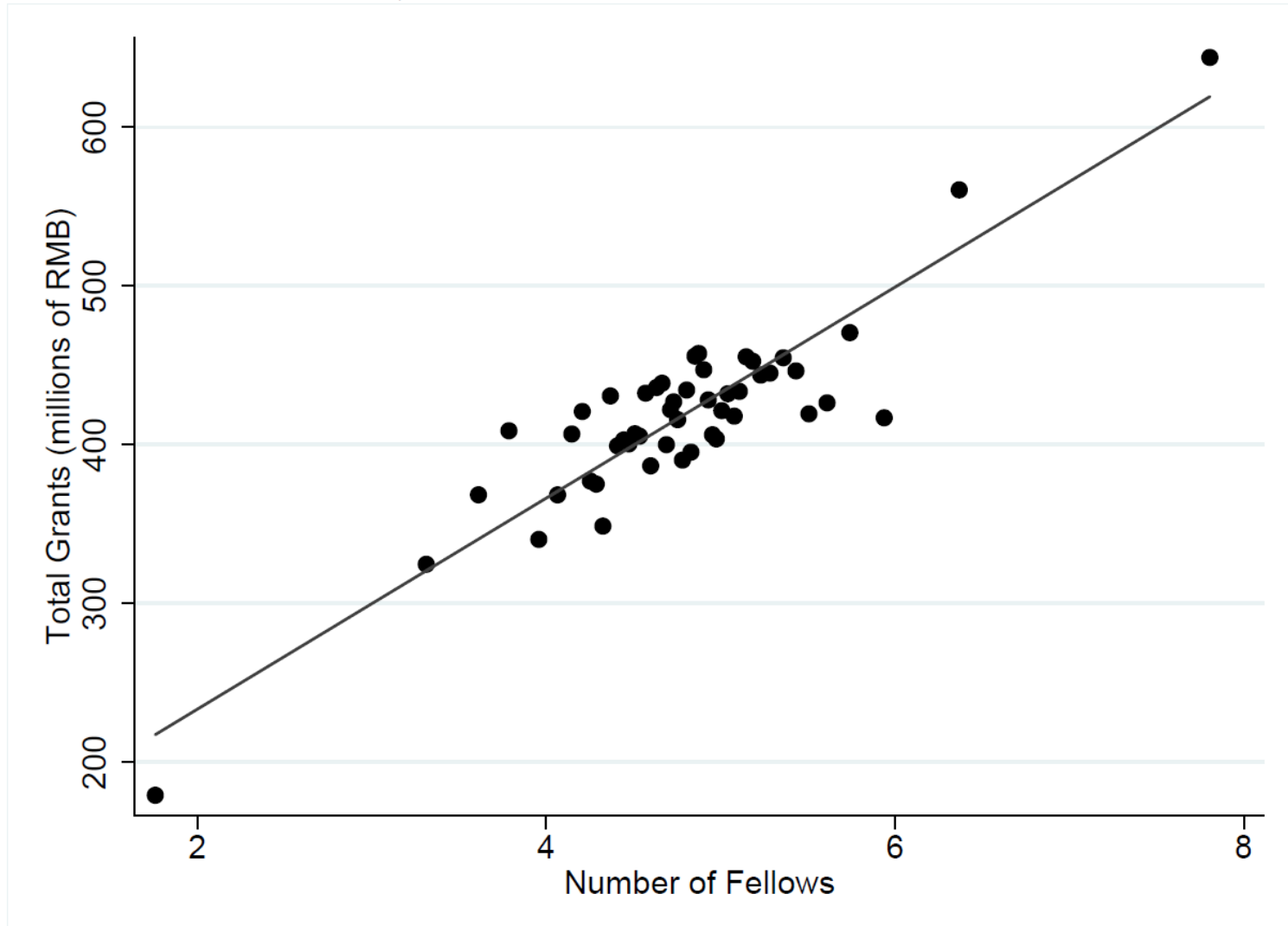
Hometown ties and *guanxi*

- “The cultivation of hometown ties is part and parcel of the Chinese culture of establishing *guanxi*, or relationships of mutual obligation between individuals, and is therefore also an inherent part of the social structure in which doing business in China is embedded at present. Moreover, ethnic Chinese communities abroad have usually preserved a distinctly Chinese cultural identity which is centered on the sharing of roots in the hometown” (Leo Douw)
- “Hometown ties are among the most common and distinctive bases for *guanxi* to build upon” (Chen and Chen)

The Chinese Academies

- CAS and CAE represent the highest honor for Chinese scientists
- Enjoy similar benefits to vice-minister level officials (e.g., access to elite hospitals)
- Given resources they control, universities are often willing to offer salary premia in the hundreds of thousands (dollars) to attract them

University funding and CAS/CAE



CAS/CAE structure

- Organized by department:
 - **CAS** Math and Physics; Chemistry; Biological and Medical Sciences; Earth Sciences; Tech Sciences, Info Tech
 - **CAE** has 9 departments: Engineering Management; Energy and Mining Engineering
- Department composition (fellows ≥ 80 have no voting rights)
 - 62-103 fellows below age 80 for CAS
 - 35-93 fellows below age 80 for CAE

CAS selection procedure (CAE similar)

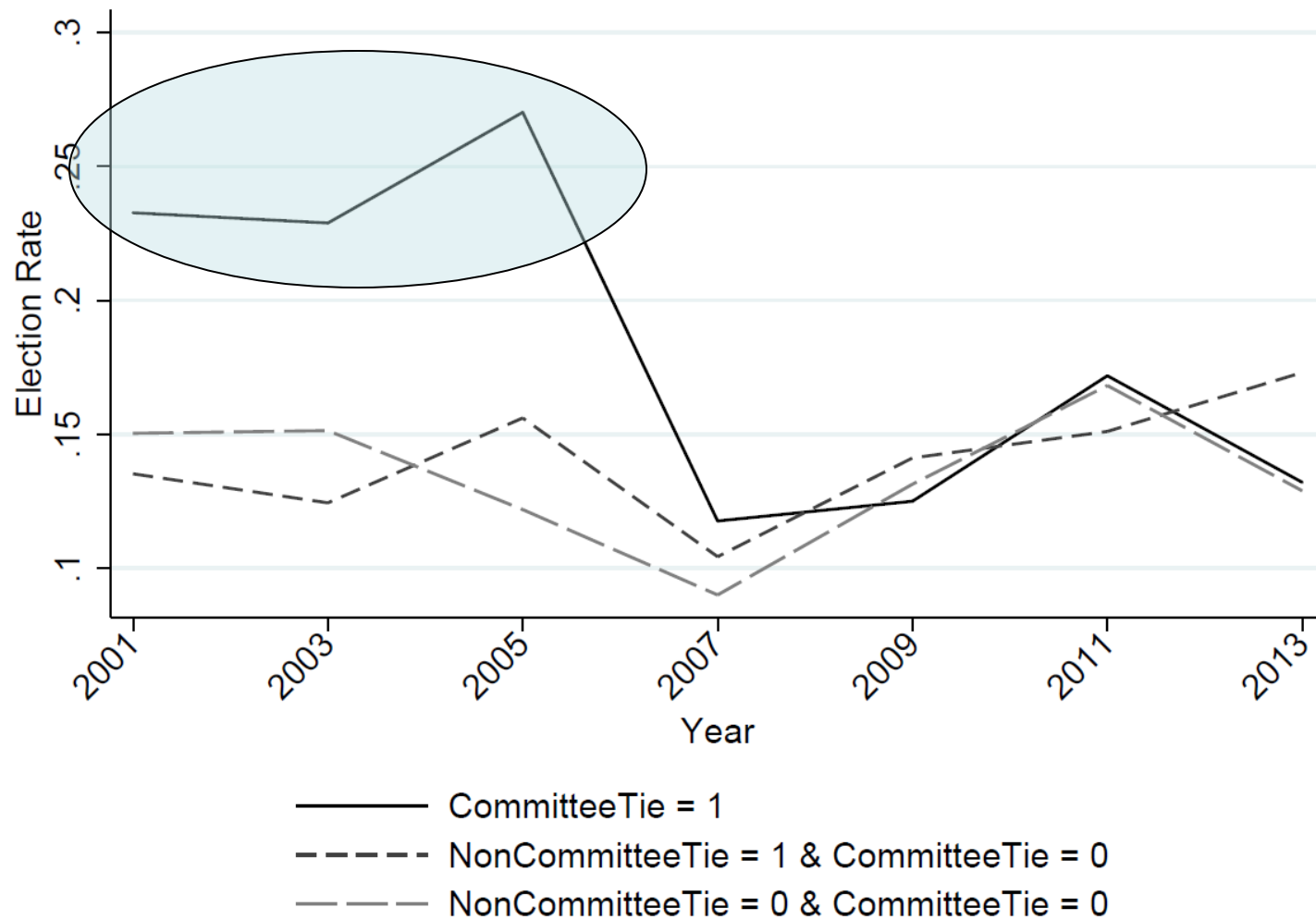
- Up to 60 new fellows selected in biennial elections in odd years
- Selection is done at the department-level, organized by its main governing body, the **standing committee (SC)**
 - Comprised of 12-23 fellows, nominated and selected by fellows within each department

CAS selection, continued

- *Nomination*
- *Stage 1: Written evaluations and voting*
- *Stage 2: In-person discussion and voting*

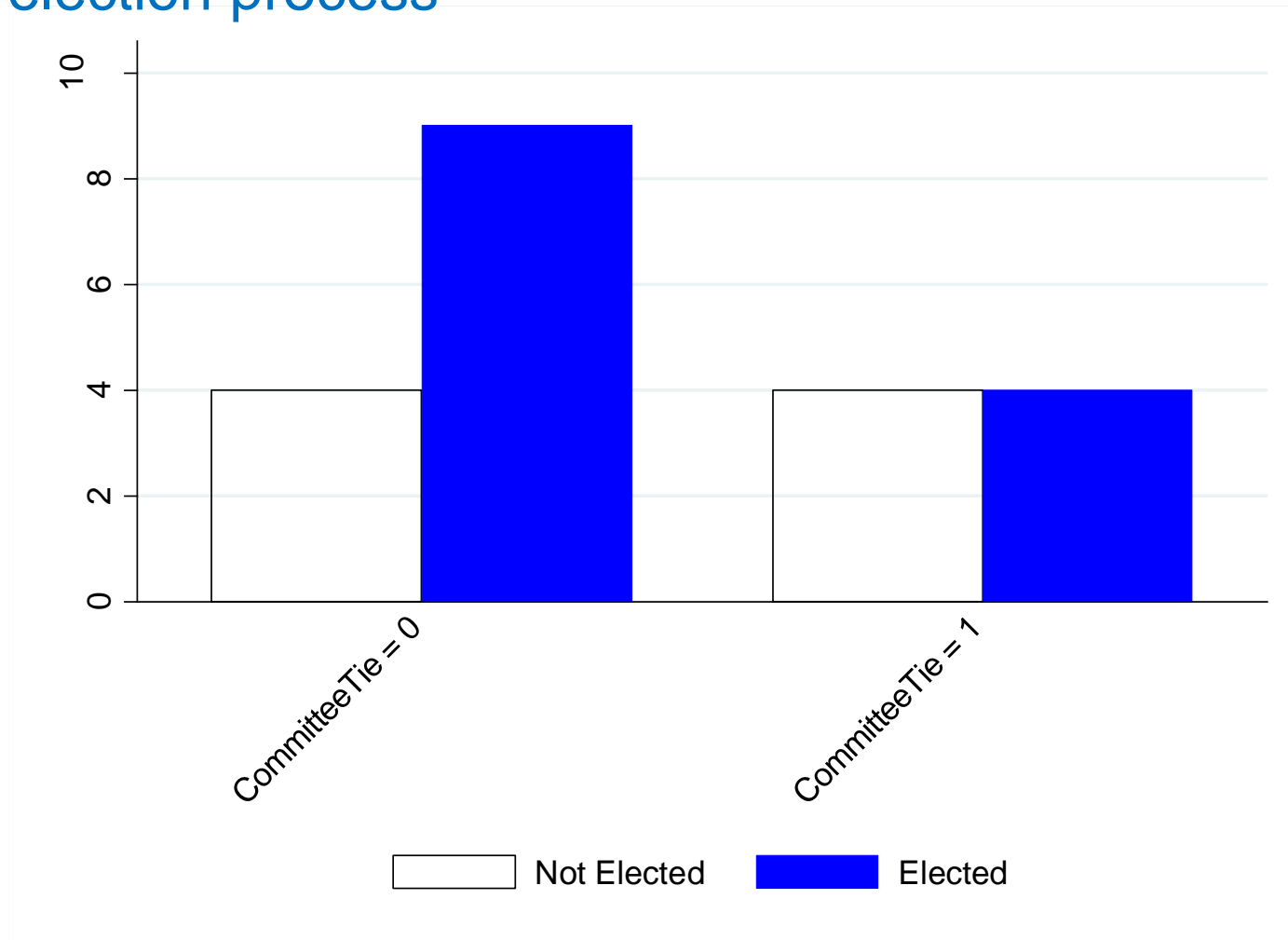
Preview/Summary of results

A CAS/CAE nominee is much more likely to be elected if he has a hometown tie to his field's CAS committee



Preview/Summary of results

No positive selection for connected nominees
in election process



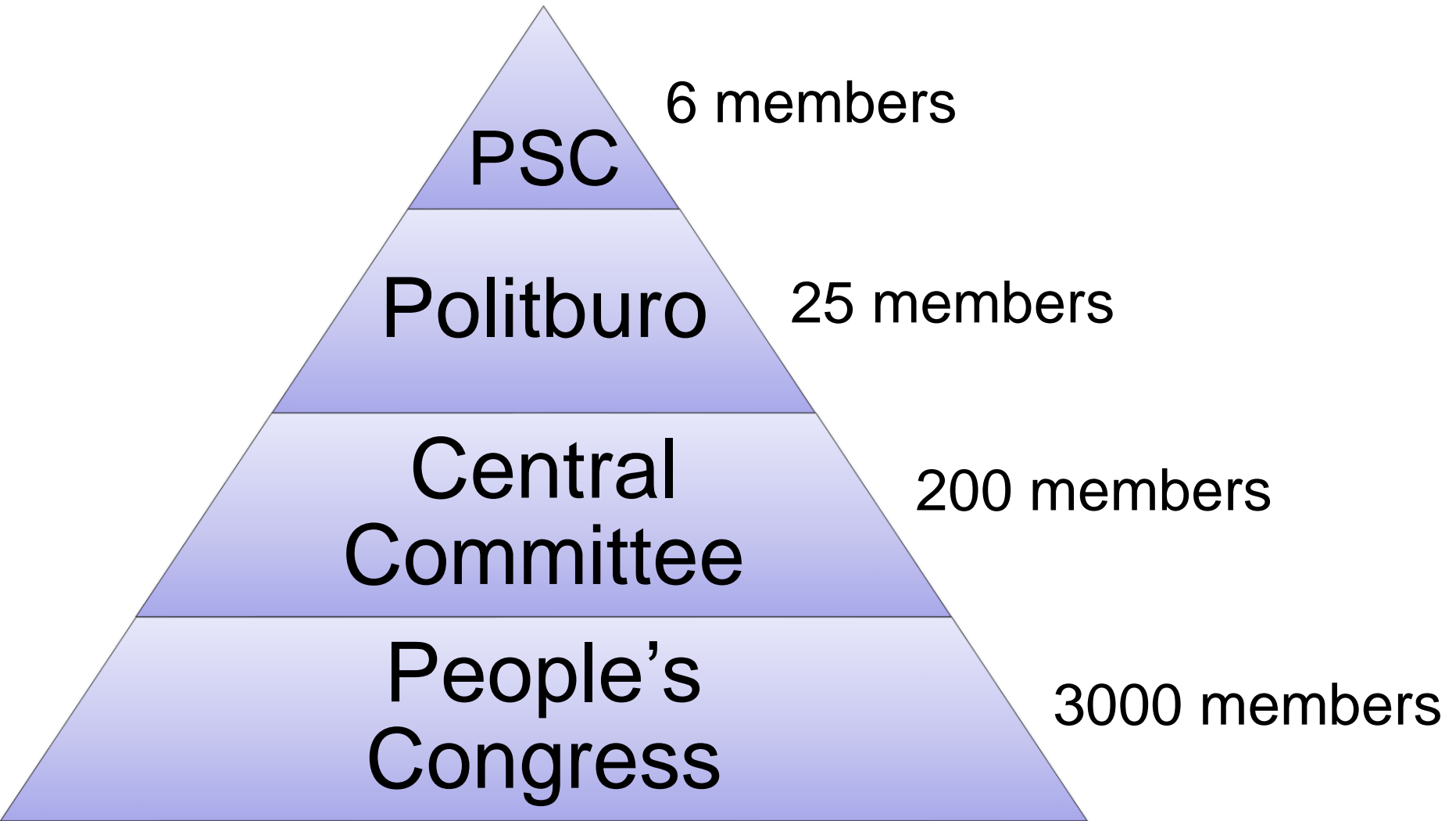
Favoritism in Chinese science – summary

- Social ties are associated with a very large increase in CAS/CAE election probability and a disappearance of positive selection
- We might care about misallocation in this domain in particular given the role of innovation in promoting longer-term development

Social ties and politburo selection

- Measurement
 - Hometown (and college) ties
- Outcome
 - Promotion to the politburo from the pool of candidates (Central Committee members)
- Identification
 - Turnover on the Politburo and its standing committee

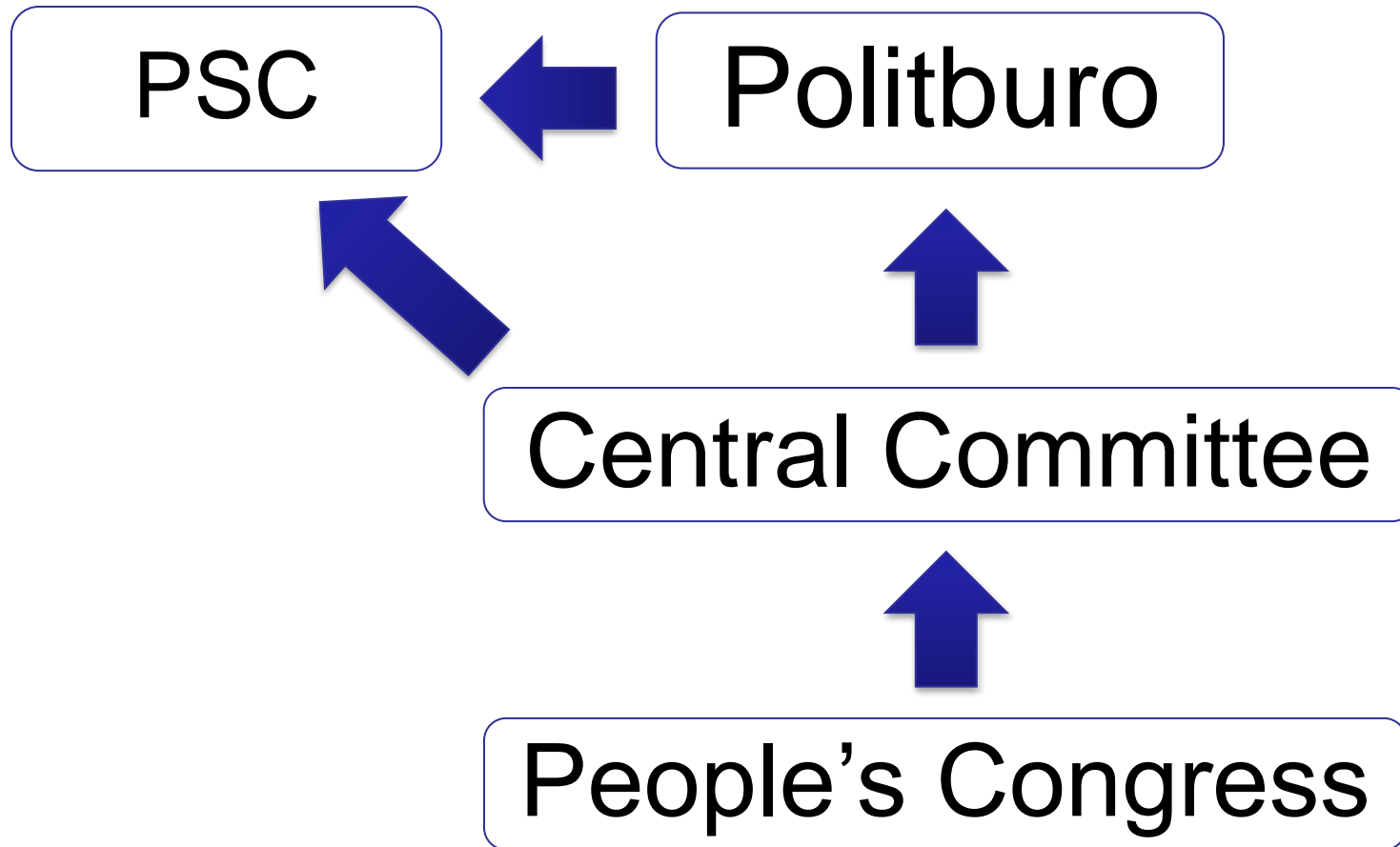
China's central government hierarchy



China's central government

- Central Committee meets annually (at least) to discuss broad government policies
- The de facto leadership resides with the Politburo (“the leaders of the Party and the People’s Republic of China”) and in particular the Politburo Standing Committee, who are drawn from the Politburo membership

Selecting China's elite, in theory



Picking China's leaders, in practice

- “[T]he notion that the Central Committee “elects” the Politburo is something of a fiction” (Li, 2008)
- In practice, it follows a “single candidate election rule” – selection is opaque and thought to be heavily influenced by Politburo incumbents (who are essentially always reelected)

It's not what you know...

- “[Politburo selection] revolves around the distribution of seats among personalistic factions - the networks of loyalty between senior political figures and the officials who have **worked with them, are from the same region or studied at the same university** and who have risen through the ranks with their patrons.” (Shirk, 2012)
- Extensive documentation of connections playing a role in lower-level promotions (though we will argue shortly that some of their empirics may be misspecified)

The party line on social ties – avoid favoritism!

It is harmful to both the individual and the collective “to let things slide for the sake of peace and friendship when a person has clearly gone wrong, and refrain from principled argument **because he is an old acquaintance, a fellow townsman, a schoolmate, a close friend, a loved one, an old colleague or old subordinate.**”



Anti-factionalism under Mao and Deng

- Mao in fact inveighed against many forms of factionalism throughout his rule
- The anti-factionalist mantle was, to some degree, taken up by Deng, continuing to denounce in-group favoritism as a danger to the party

Main result – anti-favoritism

	Elected to Politburo							
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
CityTie	−0.062 (0.021)				−0.051 (0.019)			
CollegeTie		−0.109 (0.038)				−0.093 (0.034)		
WorkTie			−0.003 (0.013)				−0.004 (0.013)	
CityorCollegeTie				−0.074 (0.023)				−0.069 (0.022)
Individual controls					Yes	Yes	Yes	Yes
Term fixed effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Hometown fixed effects	Yes			Yes	Yes			Yes
College fixed effects		Yes		Yes		Yes		Yes
Workplace fixed effects			Yes				Yes	
Observations	2,118	1,357	2,176	1,954	2,118	1,357	2,176	1,954
R^2	0.109	0.209	0.305	0.234	0.212	0.327	0.386	0.311

Social ties and elite selection – summary

- We find overall that connected Central Committee members are *less* likely to be promoted to the Politburo
- It emphasizes again that different considerations arise depending on the specifics of the setting...

Social ties and elite selection – summary

- In this case, once we introduce *organizational* considerations, there is a wider range of social relations in which exchange is embedded, and these may have diverse consequences for the role of social ties
 - Minimizing social dissent (as in Mao's view)
 - Inter-group competition
 - Intra-group competition

Social ties – the big picture

- Social relations matter for economic outcomes!!
- But they matter in interesting and complicated ways
- If we're to understand individual exchange in markets or organizations, you need to consider the social settings in which they are embedded