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On the Relevance of Identities, Communities, Groups and Networks to the Economics of Poverty Alleviation

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Forthcoming in Christopher B. Barrett (editor),
The Social Economics of Poverty: Identities, Groups, Communities and Networks
(London: Routledge)

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"Most of the people in the world are poor, so if we knew the economics of being poor we would know much of the economics that really matters."
- T.W. Schultz (1980)

I. Why Social Economics?

As T.W. Schultz asserted in the opening sentence from his 1979 Nobel Lecture, perhaps the most vexing riddle in economics is why some people remain very poor for long periods of time, and why poverty persists across generations. Canonical growth models do not offer convincing explanations of such patterns because the poor should have every incentive to invest in (human and physical) capital accumulation and to adopt new technologies to improve their lot. Recent efforts to resolve this riddle largely rely on assumptions about exclusionary mechanisms that restrict certain groups' ability to finance investments, to enjoy the external economies of scale resulting from others' investments, to cooperate, or some combination of these. Of course, this trick merely displaces the riddle: why are some people excluded and others not? Conversely, why do some people enjoy access to scarce resources or the efficiency enhancements associated with cooperation when others do not?

This book aims to advance economists' understanding of such questions by exploring how individuals' social and moral identities affect their membership in communities, groups, and networks, how those identities and social affiliations affect microeconomic behavior, and how the resulting behaviors affect poverty. Humans do not live in isolation: their behavior depends on the relations that shape their world. Variation in relationships can perhaps lead to predictable variation in behaviors and economic outcomes, which, in turn, affect social relationships through subtle feedback mechanisms. Partly as a consequence, the dynamics of human social interactions and the effects on persistent poverty have become a very active area of economic research.

The link between human relationships and behavior can operate through any of several different pathways. We highlight the effect on preferences, rules, and expectations. Individual preferences are not immutably given *deus ex machina*. Rather, they adapt within the communities to which these individuals belong. Nor are preferences over exclusively material things. People value social relationships (including deviance or conformity), fairness, integrity, friendship, love, *et cetera,* and their behaviors manifest the valorization of the non-material (see, for example, Henrich *et al.* 2004).

Not only preferences but also the rules and expectations governing individuals' interactions are shaped by formal groups and informal networks, be it in contracting for goods and services, in supporting others who suffer adverse shocks, in communicating potentially valuable information, or other interpersonal phenomena. The "ties that bind" create very real constraints on individual choice.

In affecting preferences, rules, and expectations, social forces thus affect both individuals' incentives and the constraints that they perceive. Individuals care not only about pecuniary rewards, but also prestige, stigma, and fairness. This has implications as well for prices, incomes and other monetary markers of well-being. Whether by influencing preferences or the constraints faced by individual decision-makers, the social and moral milieu in which choice occurs plainly matters, as the chapters in this book demonstrate.

Furthermore, outcomes affect individuals' endogenous construction and reconstruction of the social environments in which they place themselves or from which they extricate themselves. By changing the costs and benefits of making or maintaining contacts, economic performance necessarily induces updating of the attributes that define identities and communities and of the formal and informal matching processes that define groups and networks. This feedback between individual and group behavior injects a richness into analysis that is too often absent in social science research based excessively on either methodological individualism or cultural determinism. Durlauf and Young (2001, pp. x-1) identify recent advances in this genre as the start of "a new social economics paradigm … [that] holds the promise of providing new insights into social and economic dynamics through the explicit study of the interactions that link individual behavior and group outcomes."

This collection of papers is distinctive in its common focus on persistent poverty. Each of the contributors applies the tools of the nascent social economics paradigm to that most vexing question of economics: why poverty persists in a world of abundant resources. The chapters thus illustrate how the new insights offered by social economics might inform and improve the design of policies intended to reduce the incidence and duration of poverty around the world.

In this introductory chapter, I begin by highlighting the broad issues in economics and the social sciences to which this volume speaks. Then I draw brief thematic connections among the individual chapters. Thanks to a generous grant from The Pew Charitable Trusts, through the Christian Scholars Program at the University of Notre Dame, the team of 15 contributors to this volume held two extended workshops. In the first workshop, we discussed general ideas regarding economists' understanding of the nature of the human person – the organizing theme of each of the eight disciplinary teams organized by Notre Dame's Christian Scholars Program. In the second, we discussed and critiqued early drafts of the chapters that comprise this volume.

II. The Broad Issues

Economic behavior is embedded in a socio-cultural context, although the discipline of economics has been relatively slow to acknowledge this in its models of human behavior. Textbook models posit individuals with immutable, exogenous preferences that reflect no concern for others. Constraints depend only on endowments, technologies, and markets. Economic theory is too often taken to be truly universal in all of its details, although many of the assumptions fundamental to mainstream theory are socio-culturally specific and lack empirical support elsewhere, perhaps especially in poor communities throughout much of the world.

By studying behaviors in communities where the textbook models do not seem to fit as neatly, the contributors to this volume hope to improve not only the relevance of economic research to poor communities, but also the foundational theory and methods of the discipline. We aim to enhance economists' capacity to understand and explain how individuals perceive and adapt their identities and social affiliations and how these identities and affiliations shape social organization and affect the consumption, production and exchange behaviors that constitute economic life.

This effort echoes other recent advances within economics. Behavioral and experimental economists have made great strides in highlighting the inconsistencies between models of pure rational choice and observed human behavior, emphasizing the role of social norms (e.g., of fairness), bounded rationality and behavioral anomalies in understanding microeconomic behavior (Kagel and Roth 1995, Rabin 1998, 2002, Fehr and Falk 2002). The burgeoning fields of behavioral and experimental economics draw heavily on psychology, remaining tightly focused on individual behavior. This volume builds on the rapidly expanding literature in behavioral and experimental economics but aims specifically to situate economic behavior within human communities. In this sense, the work reflected here links closely to cognate disciplines of anthropology, political science and sociology and to ongoing debates across the social sciences.[1]

There have been numerous earlier efforts in this direction. For example, non-cooperative game theory has now become a nearly universal language for analyzing the strategic interactions that occur among non-anonymous individuals. Advances in evolutionary game theory have been used by both

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[1] See, for example, the fascinating January 2004 special issue of *Journal of Economic Behavior and Organization*, on "Evolution and Altruism", featuring a target article by the anthropologist Joseph Henrich and a series of comments by experts from a range of fields.

economists and biologists to try to explain seemingly selfless acts and the maintenance of cooperative equilibria in systems that appear vulnerable to manipulation by self-interested agents. By explicating mechanisms of direct and indirect reciprocity, many studies in this strand of the literature effectively serve "to take the altruism out of altruism" (Axelrod 1984, Frank 1988, Bester and Güth 1998, Nowak and Sigmund 2000). One of the core points of this vein of research is that welfare-enhancing, cooperative outcomes can be achieved thanks to the complex web of interrelationships that define real societies.

Formal models of interactions among individuals have likewise been used to explain the exercise of coercive power by one or more agents against others (Akerlof 1976, Basu 1986, Bardhan 1991, Naqvi and Wemhöner 1995). The key insight of the economic literature on coercive power is that networks of more than two agents can endow some individuals with the capacity to (covertly) coerce others into accepting exchanges that predictably leave them worse off and that they would never voluntarily undertake were the powerful member of the network unable to manipulate third parties.

Another strand of the literature that takes a richer view of human relationships than that traditionally considered in economics is the work on social capital. The social capital literature, which began with the theoretical work of sociologists James Coleman and Mark Granovetter and economist Glenn

Loury, treats social networks and social spillovers as *resources* that affect an individual's ability to obtain an education, secure a job, obtain credit, and enforce contracts. After a decade of intense empirical work in this area, there is today a sense that the social capital literature is taking the wrong path to address a real omission in mainstream economics. The Nobel Laureate Ken Arrow (2000) summarized this concern when he wrote: "The concept of measuring social interaction may be a snare and a delusion. Instead of thinking of more and less, it may be more fruitful to think of the existing social relations as a preexisting network into which new parts of the economy … have to be fitted." The contributors to this volume would go one step further, emphasizing that social relations are endogenous and dynamic elements of the social systems that underpin economic behavior. Economists need to study more carefully the micro-level processes that generate demonstrable correlations between particular social configurations and material outcomes – such as income, educational attainment, resilience to shocks, traders' profitability or propensity to adopt improved technologies. A new frontier of work addresses the question: What makes some social states stable, while others are unstable and therefore transient?

Our common approach to these issues begins with the observable attributes of individuals, what psychologists label "identity." Collective, shared identities – according to ethnicity, gender, lineage, occupation, race, residential location, wealth status, or some other dimension – create communities. Indeed, the word "community" originates with the Latin *communis*, meaning "shared by all or many". Shared identity can lead to salience. Particular attributes become prominent once a population evinces some critical mass that causes people to sort people using that criterion, whether consciously or unconsciously. This sorting may foster affinity among people, causing them to choose to associate with others sharing similar attributes, whether formally, in groups, or informally, in networks. The absence of shared identities,can also affect behavior, leading to alienation and social exclusion.

Because individual identities are both cause and consequence of group affiliation, social networks, and the moral codes associated with groups and networks, identities may co-evolve in ways that make it difficult – and perhaps misleading – to separate individual and social level phenomena. The joint determination of many individual attributes and of the social structures that depend on the affinity and alienation induced by identities makes it difficult to isolate the impact of particular attributes or relations, as emphasized in the burgeoning literature on the empirical analysis of social interactions (Manski 1995, Brock and Durlauf 2000, Manski 2000).

Social identity is multidimensional: an individual can belong to multiple communities, groups and networks. Interlocking networks and groups may reinforce the alienation of some subpopulations and contribute to the persistent poverty of certain social groups; or they may bridge divides. The multidimensional nature of identity is central to understanding social and economic polarization – who feels affinity for whom and who is alienated from whom – as well as the intensity of these positive and negative relations between individuals.

Two core questions emerge naturally from this formulation. The first concerns the evolution of social organization. How do communities, groups and networks form, evolve, and interact? Why do dysfunctional social relationships emerge and what causes them to persist? How should economists define and measure identities, communities, groups, and networks for the purpose of placing individual behavior in its appropriate social context?

Second, how does social organization affect economic outcomes: incomes, information flow, expenditure patterns, productivity, transfers, contracting forms, technology adoption, etc.? Here, the methodological advance of social economics meets the practical concerns of poverty alleviation and social justice. Does the social organization of individuals matter to the welfare of the poor? Does it affect what policy tools are available to and useful for outsiders who might wish to assist disadvantaged people? This is a much richer approach to understanding how socio-cultural context affects economic outcomes than the sort of scalar-valued stock concept at the root of much of the current empirical work on social capital. Recent theoretical advances – such as the multi-community social interactions model — derive the membership of communities and the nature of local social capital. This literature demonstrates the possibility that market forces may lead to communities with very different levels of social capital, exacerbating initial inequalities among individuals (Benabou 1996, Hoff and Sen 2005). The promise of social economics is that by marrying the methodological rigor of the economics toolkit with the insights of empirical anthropologists and sociologists, real progress can be made in uncovering some of the structural mechanisms that lead to persistent poverty.

III. Key Thematic Connections among the Chapters

The next 14 chapters tackle these two core questions about the nature and evolution of equilibrium social organization and the consequences for economic outcomes. Several themes appear repeatedly: identity and conflict, social norms, and the nature and formation of groups.

Identity and conflict. Following the seminal work of Esteban and Ray (1994), Akerlof and Kranton (2000) and Platteau (2000), several chapters emphasize the role of social and psychological identities in trapping individuals in poverty. Fang and Loury (chapter 2), Dasgupta and Kanbur (chapter 6), Akerlof and Kranton (chapter 8), and Barrett (chapter 9) study the emergence of individual identities that critically shape behaviors that subsequently reinforce those identities. Moreover, following the identification-alienation framework introduced by Esteban and Ray (1994), identities by multiple individuals create not only communities but, equally, alienation of individuals and groups from one another (at least partly) on the basis of within-group identities. Such alienation can lead to distinct behavioral equilibria and polarized outcomes. Duclos, Esteban and Ray (chapter 3) explore the conceptualization and measurement of these patterns in unprecedented depth, illustrating their new measure through the empirical study of polarization in 21 OECD economies.

The economic outcomes that result partly from social identification may in turn become an important dimension of identity, reinforcing patterns of alienation and identification. The key insight of this subset of chapters is thus that the feedback mechanism between identity and individual and group behavior can generate multiple equilibria. The chapters consider a variety of outcomes and social contexts: poor performance in school, low rates of adoption of improved production technologies, the limited provision of local public goods, and others. Although such outcomes are Pareto-inferior to available alternatives, the behaviors that lead to undesirable outcomes can prove individually rational given the reinforcing feedback loop created by the social context in which individuals make behavioral choices. The phenomena that these chapters describe cannot be easily explained using conventional economic models.

Ethnic, racial and religious conflict is an especially troubling manifestation of the feedback between identity and behavior and the consequences of resulting socio-economic polarization. Notions of identity are shaped by economic outcomes, such as wealth distributions, that affect subpopulations' affinity for others in their community and alienation from those in other communities – where communities are defined by shared, endogenous identities one can distinguish by some measure of social distance. Dasgupta and Kanbur (chapter 6) show how polarization can breed inter-group conflict, using a different technique to reinforce points made previously by Esteban and Ray (1999). Violence and social instability can result from group enforcement of identities shared with only some others within a population. One of the subtle subthemes to those chapters is the prospective importance of meta-communal public goods – for example, national identities forged around palpable symbols of national unity, such as an Olympic team, a flag or a national anthem – in reducing multi-dimensional social distance and thereby helping to bridge communal divides.

Social norms. A second core theme of this volume concerns the emergence of social norms that can perpetuate absolute and relative deprivation. Social norms and other conventions emerge from the aggregate behavior of individuals myopically influenced by their social identities. Blume (chapter 4) and Bowles (chapter 5) use evolutionary game theoretic techniques to study the evolution of social norms and the persistence of inequality, respectively. They show how social interactions can lead to durable community norms, some of which may prove exclusionary for some subpopulations. Such norms reflect mutual best responses conditional on individuals' beliefs about others' behavior. There typically exist, however, many possible equilibria, making it difficult to explain the emergence of any particular one and suggesting that there exist multiple tipping points that can lead to rapid shifts between states, what ecologists call "punctuated equilibria." Both Blume and Bowles emphasize that coordination failures need not result from individual myopia and that low-level equilibria can persist for long periods, even if agents are patient.

Carter and Castillo (chapter 11) empirically document some of the claims that Blume and Bowles advance. Using an unusual data set that blends conventional survey data with experimental results that gauge individual survey respondents' adherence to norms of altruism and trust, Carter and Castillo test whether those characteristics help explain the differential recovery of Honduran households from the damage wrought by Hurricane Mitch. They find strong evidence of persistent social norms of reciprocal and altruistic transfers reinforced by endogenous social interactions. Moreover, these social safety nets favor a subset of relatively privileged households. Their analysis warns against the naive belief that community norms of mutual assistance are equally accessible to all.

Goetghebuer and Platteau (chapter 15) offer a fascinating account of the feedback mechanism between identity, group membership and resource allocation in rural Peru. Under traditional property rights regimes, access to land in their study site in rural Peru is reasonably uniform and guaranteed by the social identity that makes one a part of a distinct group, while use of corporate assets, such as land, validates group membership. There results a self-reinforcing equilibrium. Goetghebuer and Platteau study the endogenous evolution of these feedback effects in the face of increasing land scarcity and emerging economic options that shift the institutional mechanisms underpinning resource allocation. Individualization of land tenure and the rise of town-based employment requiring migration combine to reduce both the egalitarian norms that traditionally characterized land allocation and younger adults' identification with their lineage and community, perhaps especially among poorer families.

Thus identities, groups and resource allocation mechanisms coevolve and may do so differentially across economic classes.

Hoff and Sen (chapter 7) study another mechanism through which identities and networks can lead to persistent poverty. They develop a simple but elegant model of a kin system interacting with an expanding market economy. Members can face barriers to entering the market economy, barriers that emanate from the incentives of kin members to engage in workplace nepotism and other sorts of in-kind transfers to meet kin obligations. Facing barriers to good jobs, good housing, or other crucial means to economic advancement, a kin member's response may be to demonstrably sever his kin ties, if he can, in order to improve his modern sector opportunities. That possibility can lead the kin group to respond in a perverse way. If the kin group foresees that it will lose some of its most productive members as the economy opens up, it may take collective action to erect exit barriers. If that occurs, then the kin system—that was once a beneficial arrangement—will become a poverty trap, at least for its most productive members.

The formation and consequences of groups. A third theme concerns the formation and consequences of social aggregates, such as informal farmer networks, trader networks, and self-help groups. Udry and Conley (chapter 10) show why "households," "firms," and other familiar units of analysis in economics may be inappropriate units of analysis in poor rural villages around the world. Using an unusually rich data set from Ghana, Udry and Conley demonstrate that finance, information, labor, and land flow through social networks that often cleave households. An individual's access to resources is typically conditioned by the network(s) to which s/he belongs, and network-mediated access is typically non-transferable even within nuclear households. The interconnectedness and complementarities among different functional networks (e.g., for information, credit, insurance, etc.) can magnify the importance of each individual link (e.g., for information). Udry and Conley make the case for studying the broad set of networks in poor rural villages, although there remain daunting identification challenges inherent in isolating networks from one another for empirical analysis.

Several other chapters offer strong evidence of the effects on economic performance of group and network membership. Fafchamps (chapter 12) studies agricultural traders in three African nations (Benin, Madagascar and Malawi). He finds that individual attributes, such as gender, ethnicity or religion, matter less to access to credit and to information – both key predictors of performance – than do the networks to which a trader belongs. Although his study takes network structure as given, Fafchamps' findings suggest that it is the relationships one purposefully builds and maintains – and not the latent relationships prospectively available due to particular shared identities – that may matter most to economic behavior and performance. Fafchamps (2004) makes the broader case that in developing and transition economies with only embryonic legal systems and considerable production risk, markets can be most usefully understood as personal networks that link firms, making possible relational contracting.

Foster (chapter 13) looks at the determinants of altruism by studying the nutritional status of women in rural Bangladesh, paying careful attention to the biological relationship between the woman and other household residents, and also to the potential selection bias arising from joint residence decisions. Foster finds not only that genetic relationships matter – for example, daughters-in-law fare less well than women biologically related to household heads – but also that individuals care differentially about family members with whom they do and do not live, even controlling for the co-residence decision. In these data, it does not appear true that distance makes the heart grow fonder. These results speak to longstanding concerns about the consequences of patrilocal residence traditions for rural women who face social constraints on activity and mobility.

LaFerrara (chapter 14) shows how the organization and performance of self-help groups in the slums of Nairobi, Kenya, vary according to the social composition of the group, and how these, in turn, affect the incomes of members.

She finds that greater within-group heterogeneity tends to lead to less specialized division of labor and less use of sanctioning mechanisms against free riding behavior. These findings reinforce the point made by others – e.g., Barrett (chapter 9) and Chwe (2001) – that homophilous groups and networks – i.e., groups whose members possess similar attributes – are more likely to foster inter-household cooperation and social efficiency in the absence of institutional structures expressly designed to manage heterogeneity.

IV. On Social Economics and the Economics of Poverty Alleviation

We thus return to the question that opened this introduction: why should scholars and practitioners concerned about poverty reduction pay attention to social economics? What can emerging research in the new social economics paradigm contribute to the practice of poverty reduction? The chapters in this volume point to at least five distinct contributions.

First, the chapters underscore the importance of social context. In many settings, it is essential to consider the identities, communities, groups and networks at play if one seeks to understand the motivations behind individuals' choices regarding the allocation of scarce resources and the standards of living that result. Economic policy operates within a complex social and moral context that varies across cultures and over time. Models are necessarily useful simplifications of a complex reality – as the statistician George Box famously declared, "all models are wrong, some are useful" – but the the reductionism that is useful for modeling one place and time may prove indefensible in another. The research in this volume underscores the caution *caveat utisor* ("user beware!") against injudicious application of models developed in one context to alternative settings.

A second, key implication of social economics is that to make policy recommendations, it is generally important to understand how identities, communities, groups and networks may change in response to interventions. Having recognized the apparent association between social capital measures and economic performance, many development agencies have been aggressively seeking out groups and networks in developing countries, and even creating new groups and networks in the hope that this will stimulate pro-poor growth. Social economics raises important questions about the likelihood of success of ventures that attempt to stimulate the emergence of new groups, versus those aimed at reinforcing pre-existing associational structures among the poor. This is a new research frontier about which we still know too little to make policy recommendations with confidence.

This raises a third and closely related point. Although it is true that social groups can sometimes resolve market failures such as imperfect contract enforcement and limited access to insurance and credit, and can thereby facilitate investment and growth, perhaps especially for the poor, so too can groups prove exclusionary, throwing sand in the wheels of progress for excluded individuals and groups. In extreme cases, exclusionary processes turn violent, with the poor suffering a disproportionate share of the resulting hardship, as vividly manifest in recurrent inter-ethnic and inter-faith violence in sub-Saharan Africa and South Asia in recent years.

Fourth, given the self-reinforcing nature of many social groupings and norms, there can be great value in efforts to create meta-identities that bridge social divides and to break down informal and formal exclusionary mechanisms that impede cooperation and accumulation within poorer segments of a society. Such exclusionary mechanisms are essential to the existence of poverty traps (Carter and Barrett 2005).

Fifth, because social organization is typically characterized by multiple equilibria, small changes in economic conditions can lead to dramatic changes in the behavior of, and membership in, groups and networks. In systems that appear to function reasonably well, this strengthens the case for public safety nets to ensure that covariate shocks associated with natural and human disasters do not so perturb existing social systems as to undermine community mechanisms, such as informal networks that provide critical mutual insurance in the face of household-specific, idiosyncratic shocks.

The application of the emerging tools of social economics to the vexing problem of persistent poverty remains in its infancy. Much remains to be learned. The chapters in this volume help to point the way toward a new era of economic research that maintains greater fidelity to the rich socio-cultural fabric of developing countries and to underprivileged communities in rich nations, and in so doing yields practical advice to policymakers and practitioners struggling to meet the challenge of poverty reduction.

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