

Bonding Together or Bridging the Gap: understanding the effect of social capital on income inequality

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Motivation

In modern American society we know that social networks matter. How these networks matter is another story. The development of social capital has been linked to positive economic growth, however, the relationship between social capital and income inequality remains unclear. Over the past several decades, not only has the U.S. seen a major decline in social capital, but it has also reached unprecedented levels of economic inequality.

Do social networks provide a means for access to jobs? Or do they stratify society into the haves and the have-nots?

Theory

H1: If social networks bridge socioeconomic divisions, then social capital will decrease market income inequality.

- Improves efficiency of job allocation by leveraging human capital and group resources
- Encourages business investment

H2: If social networks reaffirm socioeconomic divisions, then social capital will heighten inequality.

- Perpetuates labor market inequalities and inefficiencies
- Conveys disproportionate economic and political power to particular groups

Theories and Mechanisms

	Expected Relationship	Condition	Mechanism
Putnam	+	bonding SC	reduced transaction costs
	-	bridging SC	
Hero	∅		racial diversity
Alternate	+	racial homogeneity	labor market efficiency; favorable business climate
	-	racial heterogeneity	labor market inefficiency; unequal political power

Data

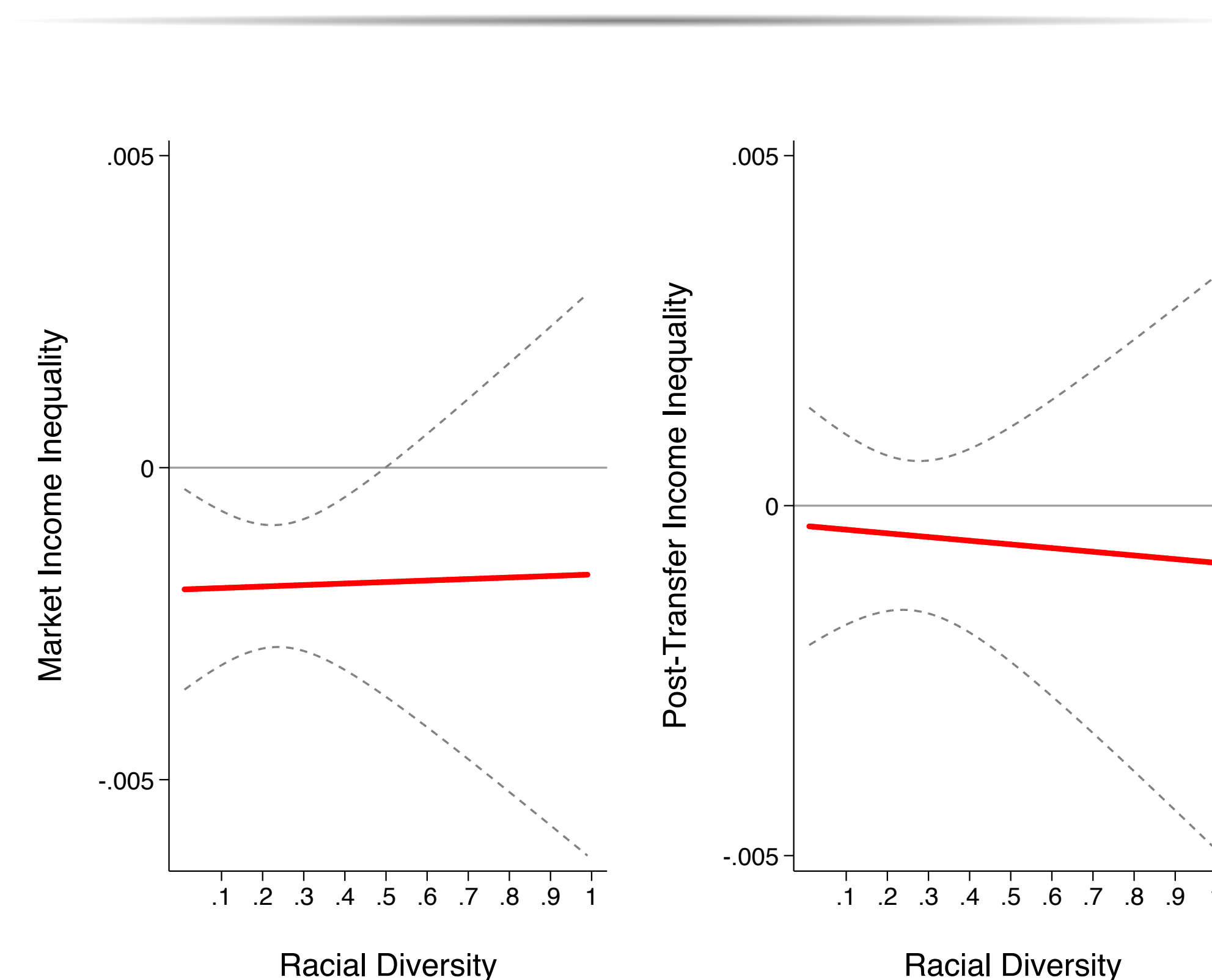
Panel of U.S. states from 1984-2006

Income Inequality: annual market-based and post-transfer gini coefficient

Social Capital: Hawes, Rocha, and Meier (2013) state-level survey-based measure

Racial Diversity: $1 - \sum_j p_j^2$ (j is racial category, p is proportion in that category)

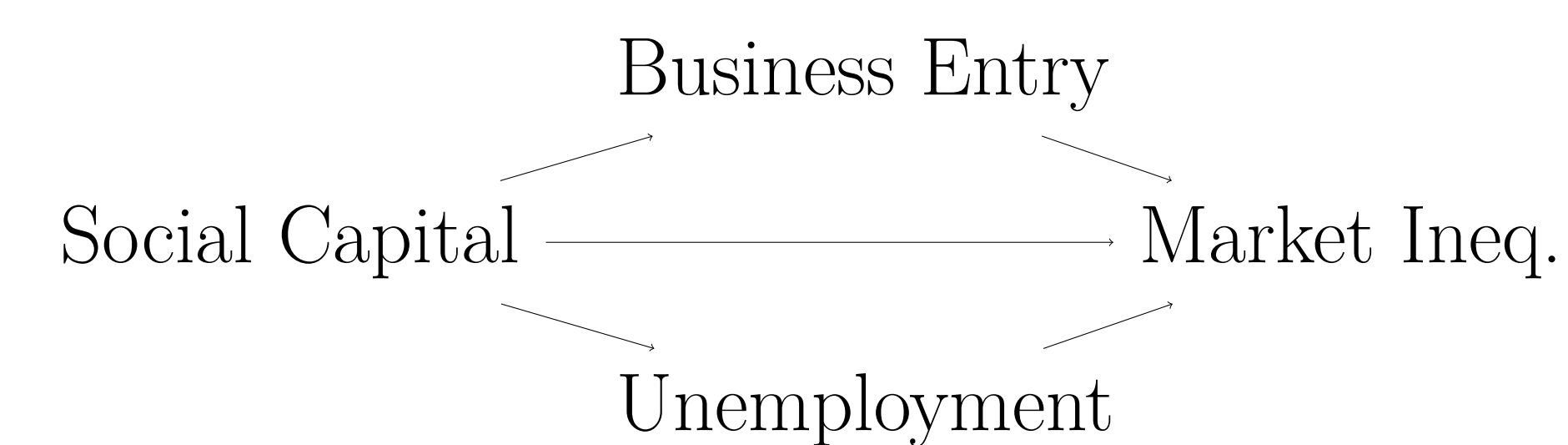
Social Capital and Racial Diversity



- In racially **homogeneous** states, high levels of social capital are associated with less *market* inequality.
- In states with high levels of racial diversity social capital has no relationship with market income inequality.
- There is no direct relationship between social capital and post-transfer inequality.

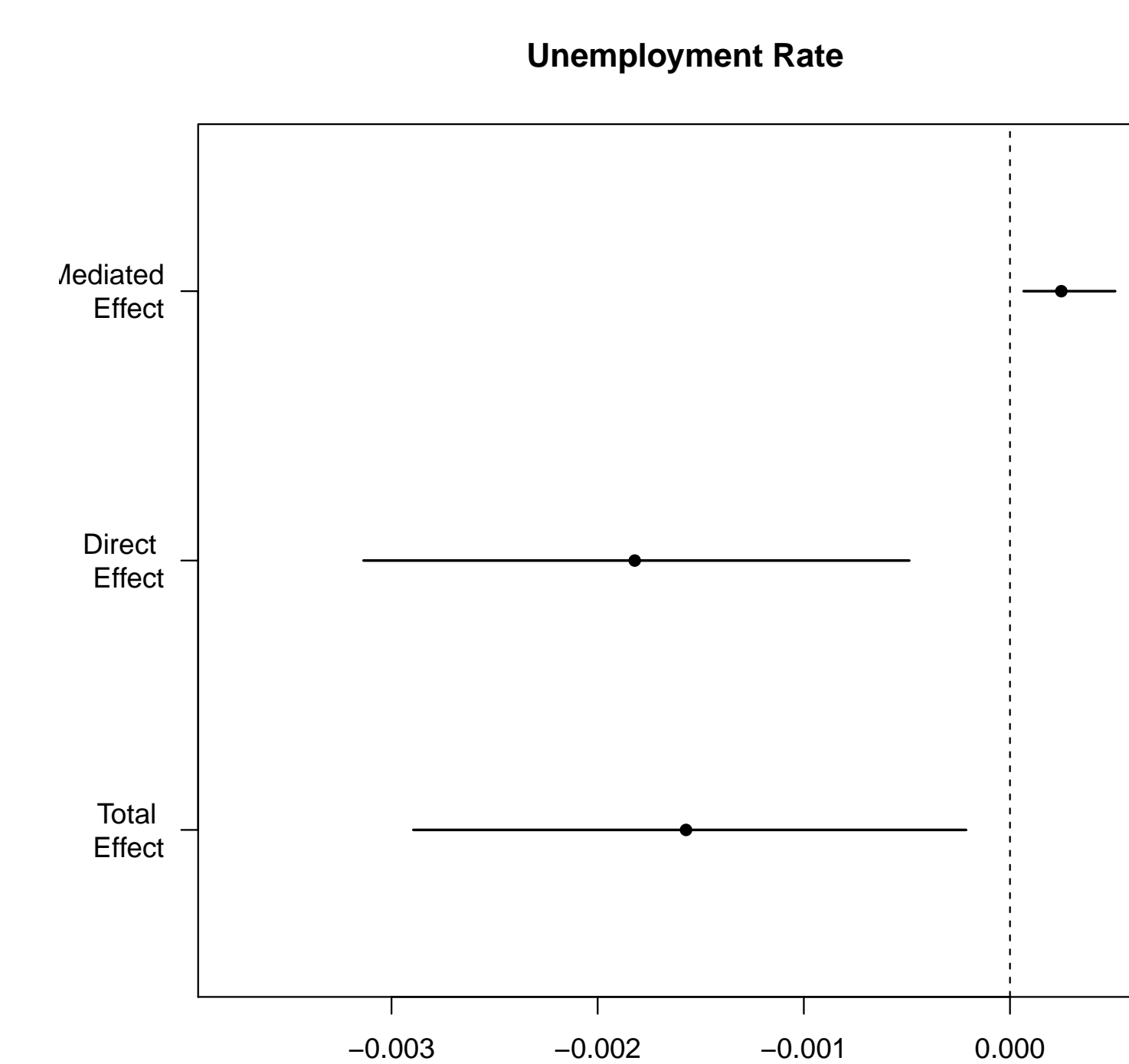
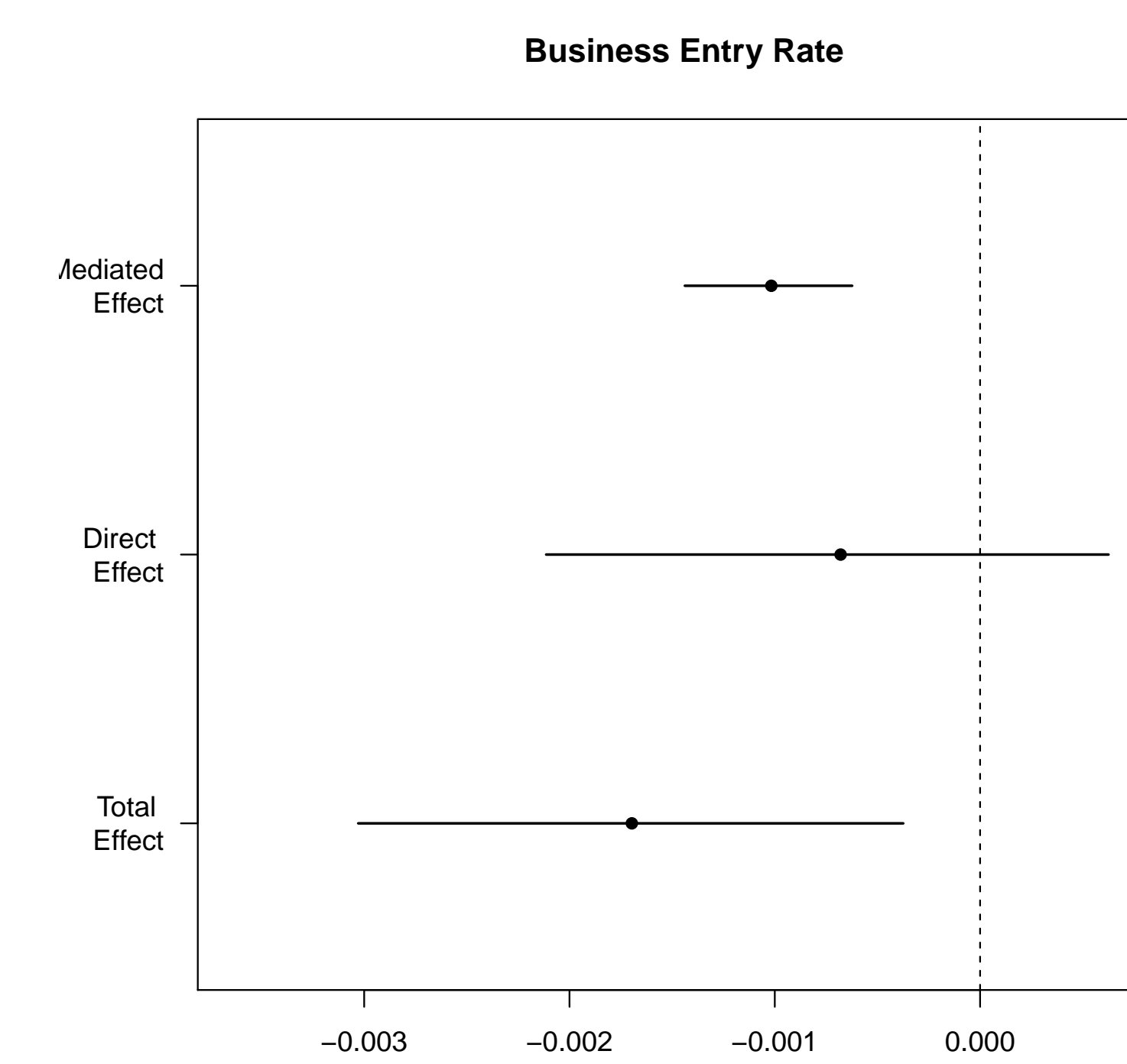
Economic Mechanisms

The level of social capital within a state can improve efficiency in the societal allocation of jobs by leveraging social networks to disseminate information.



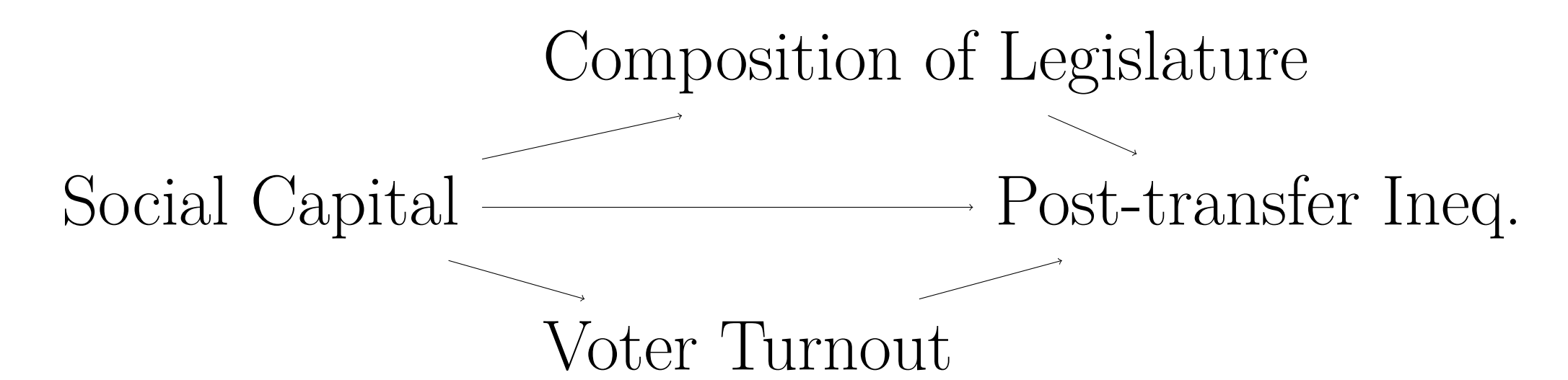
- States with high levels of social capital, ceteris paribus, are preferable to businesses because of increased ease in hiring and improved government performance.

- By increasing unemployment, likely because of the role of racial diversity, social capital can worsen (increase) income inequality.



Political Mechanisms

By reducing the transaction costs to political involvement, social capital can help to solve collective action problems, but also may confer disproportionate political power to distinct groups.



- States with more social capital are expected to have less post-transfer income inequality, because of increased political power of Republicans.

- By conferring political power on white voters, social capital is indirectly and positively associated with heightened inequality.

