

Poverty, Social Capital, and the Formation of Subjective Income Expectations*

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Poverty in America is not limited to material deprivation. It is also a psychological and social phenomenon. The stress of poverty may lead to suboptimal decision-making among the poor (Shah et al., 2012; Mani et al., 2013; de Bruijn and Antonides, 2022). Similarly, the anticipatory disutility of future poverty may shorten planning horizons (Elster and Loewenstein, 1992; Laajaj, 2017). Such gloominess about future prospects reveals a pessimism in economic expectations. Indeed, as depicted in Figure 1, low-income Americans consistently report lower prospects for growth in their future financial situations as compared to middle-income and high-income Americans.¹ These expectations matter for mobility and poverty. Low expectations of earnings growth might reduce effort, leading to a self-fulfilling prophecy of immobility (Dalton et al., 2016; Lybbert and Wydick, 2018). Similarly, increasing expectations may increase effort (Jensen, 2010).²

In many cases, poor Americans are often socially isolated from their non-poor counterparts (Durlauf, 2006; Wang et al., 2018). Such differences in social capital, in addition to income and stress, can further

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¹Data comes from the University of Michigan Survey Research Center's Surveys of Consumers, which asks respondents "Now looking ahead – do you think that a year from now you will be better off financially, worse off, or just about the same as now?"

²Of course, it should be noted that too optimistic of expectations can themselves be dangerous. Unfounded optimism could backfire in the face of realized income, leading to even greater pessimism in the future.

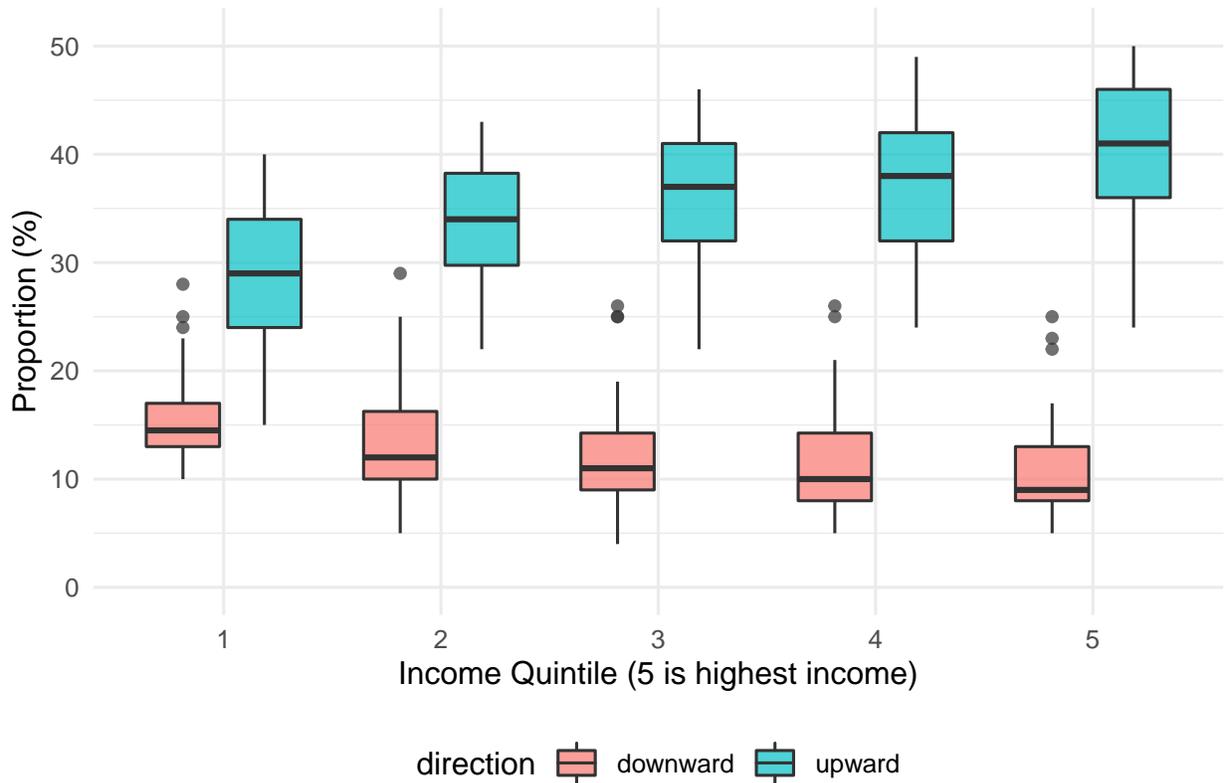


Figure 1: Proportion of respondents with expectations of upward/downward mobility by income quintile in the University of Michigan Survey Research Center Survey of Consumers. Data is yearly proportions by quintile from 1978-2022.

drive income immobility (Jackson, 2020; Chetty et al., 2022). While the role of instrumental network effects and their effect on mobility has been well explored, social capital may similarly drive expectations of (and aspirations for) future earnings.³ Social capital also buffers against stressors which could lead to a pessimistic outlook as social support networks may reduce stress by providing informal insurance or other favors (Jachimowicz et al., 2017; Morduch and Schneider, 2017). Following on the results of Chetty et al. (2022), we trace a possible mechanism for the lack of mobility in the United States, examining the formation of subjective income expectations as a function of social ties to understand optimism and pessimism about mobility.

In this project, we study the dual role of social networks and poverty in the formation of income expectations. Do poverty and social capital drive income expectations? And if so, how? To answer these questions, we elicit subjective probabilities of future income and construct income distributions from these

³See, for example, Dimaggio and Garip (2012).

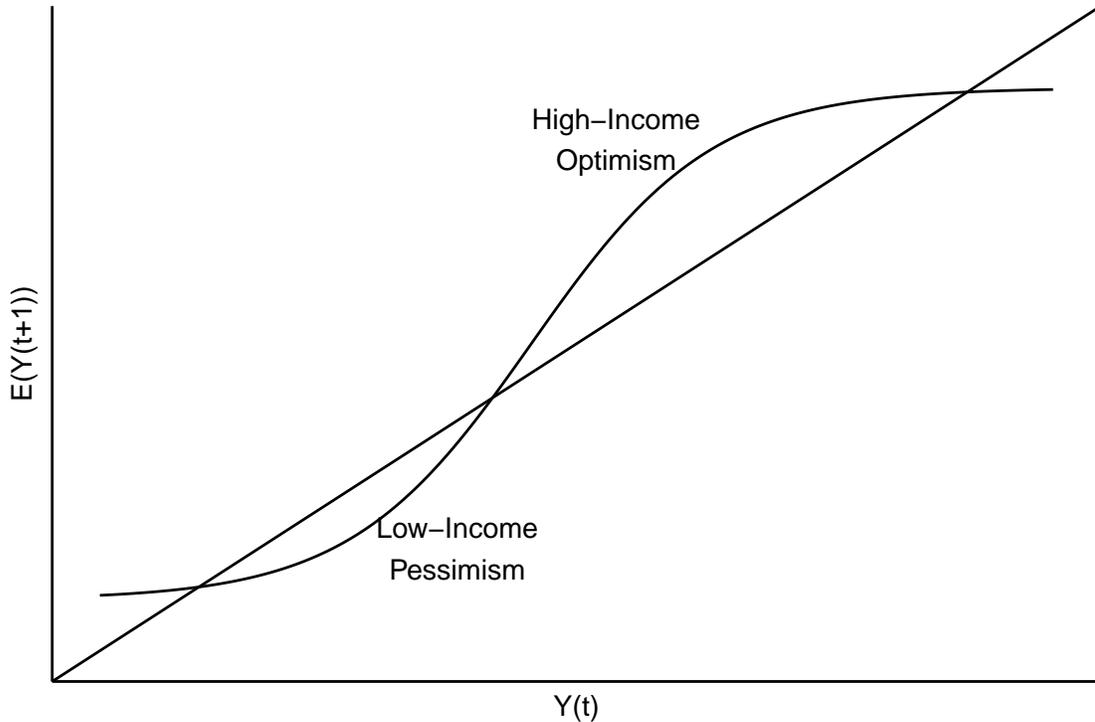


Figure 2: An S-Shaped Curve in Income Expectations. $Y(t)$ is income today, and $E(Y(t + 1))$ is expected income over the next year.

subjective expectations. First, we describe how income expectations vary with poverty. While future income expectations will naturally rise with income today, we study deviations from stable incomes, with a particular interest in “non-convex” patterns of expectations. If we observe pessimism at lower levels of income compared to optimism at higher levels of income, we will see an S-shaped curve of expectations in income. This curve is similar to that studied in the poverty traps literature (e.g., Lybbert et al.,2004; Antman and McKenzie,2007) with the distinction that the outcome is expectations as opposed to actual future income. As plotted in a hypothetical curve in Figure 2, we will empirically test for patterns consistent with such an S-shaped curve. Additionally, we study how stress, economic connectedness, and support networks might lead to the formation of optimistic or pessimistic expectations. In particular, we test if role models drive optimism and if support networks curtail pessimism among the poor.

With a nationally representative sample ($n = 6000$) in the United States, we elicit subjective probabilities of one year ahead income expectations. We over-sample those who are below 200% of the Federal Poverty Line to have greater statistical precision among low-income populations. Our subjective income expectations module is based on that first utilized by Dominitz and Manski (1997). This elicitation yields

rich, detailed information about the distribution of income expectations, and this method has been shown to produce information consistent with real-world decision-making (Delavande et al., 2011). Respondents are asked “What is the percent chance that your total household income, before taxes, will be less than Y over the next year?” and respond by dragging a slider to the appropriate probability between 0 and 100. Beyond the lion’s share of our respondents taking the survey online, we make several adjustments to the instrument from Dominitz and Manski (1997). First, we manipulate the order of income levels presented—presenting these in either descending or increasing order—and the direction of comparison—asking if respondents will one make “more” or “less” than a given amount. Second, to make the numerical probabilities more legible to respondents, we draw upon the probability expressions literature to annotate the slider (Lichtenstein and Newman, 1967; Pellissier and Van Buer, 1996; Biehl and Halpern-Felsher, 2001). To do so, we find phrasing from this literature that is well calibrated to specific numerical probabilities and fits the language of the instrument.⁴⁵

The subjective income expectations module is combined with a number of other careful survey modules to test our hypotheses about the formation of these expectations. We have information on respondents’ household incomes and sizes, stress levels (using a stress scale based on Cohen et al., 1983), economic connectedness (using questions built to mirror the measures in Chetty et al., 2022), social support, social trust, and other measures of mobility. To study the formation of expectations according to these factors, we will construct distributions within population subsets identified by these measures. Other cross-cutting themes may also be relevant including gender, race, ethnicity, geography. Given that economic outcomes differ along these lines, economic expectations may vary along these same lines.

These analyses will contribute to the burgeoning literature on psychology and the economics of poverty. In particular, our results are relevant to the predictions of models from behavioral economics (Dalton et al., 2016; Lybbert and Wydick, 2018), and the study of behavioral poverty traps. Second, our results will contribute to the empirical literature on subjective income expectations, and more narrowly, within the United States, complementing the results of Dominitz and Manski (1997). To our knowledge, ours is the first study to examine income expectations in the United States with an explicit focus on poverty. Third, with careful design of our instrument, including the use of probability expressions and a subtle survey experiment, we

⁴In particular, we annotate the scale as follows: 0%: No chance, 20%: Low chance, 40%: Moderately low chance, 60% Moderately high chance, 80%: High chance, 100%: Certain.

⁵Third, though perhaps less dramatically, we seed our algorithm based on the respondents’ current household income (as previously reported) as opposed to the midpoint of the lowest and highest possible incomes in the next year.

contribute to the measurement of subjective expectations. Variations on this method have been applied wide variety of domains including public health (Delavande and Kohler, 2009; Delavande et al., 2011) education (Jensen, 2010; Attanasio and Kaufmann, 2014), agriculture (Bellemare, 2009), and migration (McKenzie et al., 2013). Such advances in measurement may prove useful far beyond the measurement of income expectations.

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