

Peer Effects in Financial Expectations

Joshua Thornton – University of California, Irvine

Motivation

1. Beliefs affect a variety of outcomes.
 - Currency value, corporate investment, political shifts, etc.
2. Peers have been shown to influence a variety of market outcomes.
 - Stock market participation, hours worked, housing decisions, etc.
3. One cannot necessarily infer beliefs from outcomes.
4. More work is needed to understand whether peers affect underlying attitudes and beliefs.

Preview of Results

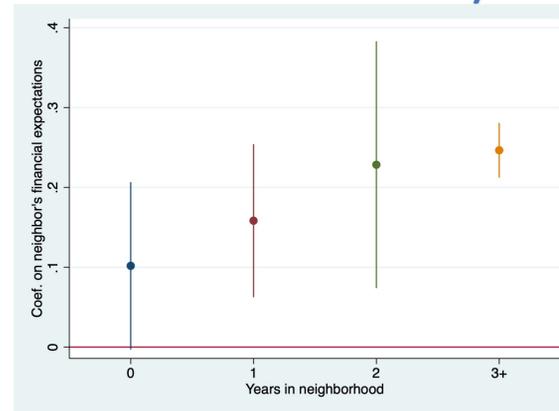
1. Individuals are influenced by the financial expectations of their neighbors.
 - A one standard deviation increase in neighborhood financial expectations leads to a 2.36% increase in an individual's financial expectations.
 - Peer effects are only significant for socially connected individuals.
2. Surveyed expectations are related to savings behavior.
 - Individuals who expect their financial situation to improve are less likely to save.
3. Individuals are making good use of information when they learn from their peers.
 - Individuals who form more accurate financial expectations display peer effects.

Identification Strategy

1. Controls
 - Individual and year fixed effects → Rule out time-invariant individual characteristics and sample wide time trends.
 - Time-Varying Controls → Wealth, job industry, education, marital status, race, political party, primary newspaper, region.
2. Instrumental Variable → I Instrument for neighborhood financial expectations with the average financial expectations of neighbor's nonlocal family members.



Reverse Causality

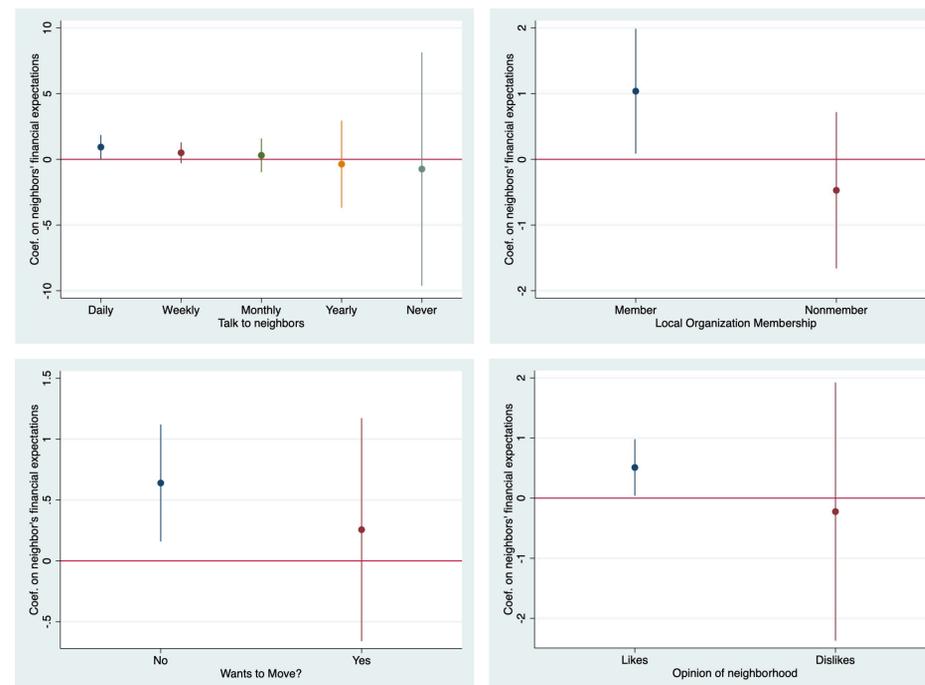


IV Regression

	Financial expectations
Neighborhood financial expectations	0.512*** (3.04)
Observations	230,868
Individual FE	YES
Year FE	YES
Time-varying controls	YES

Sociability Proxies

Common result → Peer effects are only significant for socially connected individuals.



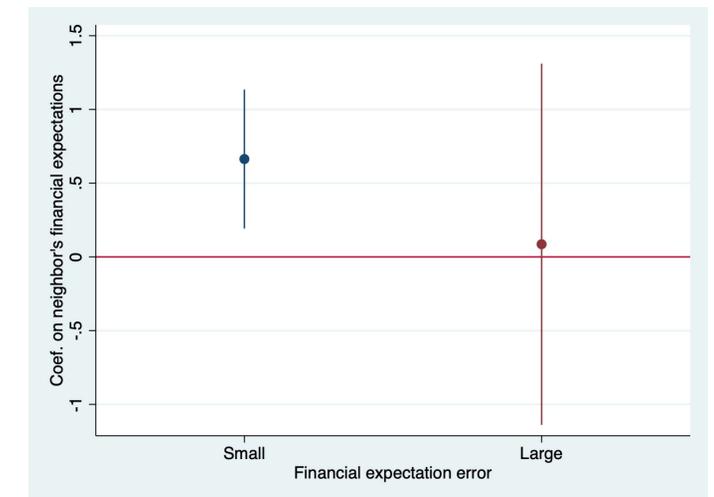
Expectations and Savings

Individuals who expect their financial situation to improve are less likely to save.

	(1) Savings dummy
Financial expectations	-0.0111*** (-5.29)
Observations	230,962
Adj. R-squared	0.361
Individual FE	YES
Year FE	YES
Time-varying controls	YES

Use of Information

Individuals who form more accurate expectations display peer effects.



Contribution

1. Peer effects literature: To my knowledge, this is the first paper to provide evidence of peer effects in financial expectations.
2. Belief formation literature: I provide evidence that individuals use the financial expectations of their peers as an input when forming their own financial expectations.
3. Household finance literature: I show that individuals who display peer effects form more accurate financial expectations.
4. Social finance literature: My results offer support for existing theoretical work on social transmission of beliefs.