CERF Fellows' Report – August 2017

*Summary*: The proposed research focuses on understanding why and in what way social interactions and peer effects are important for households' financial decisions and behaviour. In particular, is information exchange and dissemination about assets, financial products and investment opportunities among individuals important for improving their decision making process for participating in the corresponding asset or financial product markets? We provide a framework for understanding how the exchange of information about assets and financial products in a social context can improve or hinder the financial decisions of households. We hypothesize that there are two potential channels via which social interactions may generally affect investment decisions: (i) *information* peer effects, which arise from directly exchanging pieces of information with friends and acquaintances, and (ii) *imitation* peer effects, comprising of social norm effects in preferences, fads, etc. With this in mind, we will first develop a model of direct communication and social learning, within a generic financial market on a social network, where households are privately informed about assets, but can exchange private information with friends and acquaintances. We then address our research questions from an empirical perspective, in the context of large and financially developed economies. For this purpose, we exploit a data set from a survey funded by Keynes Fund and CERF, fielded in France. The survey provides measures of participation in asset markets, relative to individuals' financial wealth, but also of subjective expectations and perceptions of market and policy relevant outcomes, e.g. stock returns or interest rates, via probabilistic elicitation techniques. In addition, the dataset contains a very rich set of covariates for socioeconomic and demographic controls, preferences, constraints and access and frequency of consultation of information sources, typically absent from social network empirical studies. Crucially, the data set also contains specific questions designed to obtain quantitative measures of relevant network characteristics that enable identification of information network effects on financial decisions from individual answers. Last, the data set contains three groups of questions, one for each of the relevant financial domains: stocks, housing and debt. We develop research individually for each of these three. The findings of the proposed research are pivotal for our understanding of the role of social interactions for financial behaviour. Our research findings to contribute towards overcoming financial literacy limitations in the general population, by helping design policies that promote information exchange between individuals in a social context. Without a better understanding of how sound financial knowledge is generated (or the lack of it thereof), we cannot provide good policy recommendations that could credibly alleviate the undesired consequences of widespread financial illiteracy.

*Dissemination*: The research has been presented in various international conferences by the CERF fellow (Giannitsarou) as well as her co-authors. Some of this include the Royal Economic Society (RES), the Computing in Economics and Finance (CEF), and the summer European Economic Association and Econometric Society (EEA-ESEM) annual meetings. The fellow and one of her collaborators presented their work at the Bank of England in July at a more specialised, targeted workshop that took place at the Bank of England.

*Achievements*: The fellow has recently submitted an application for a standard grant to the ESRC, based on the pilot research that CERF and Keynes Fund funded. Also, the fellow and two of her co-authors have proposed a session for the annual winter meeting of the American Economic Association, which has now been accepted for participation.