

## **Sturm & Drang Prize 2020**

**Simon Heß: “Development Projects and Economic Networks: Lessons From Rural Gambia,” forthcoming in *The Review of Economic Studies* (co-authors: Dany Jaimovich and Matthias Schündeln)**

### **Laudation by Michael Kosfeld**

*“It’s not what you know, it’s who you know.”* This popular proverb emphasizes the great importance many of us attribute to social and economic networks in our daily life. And indeed, starting from the seminal work by Mark Granovetter in the early 70s of the last century, who documented the so-called “Strength of Weak Ties”, social science research, in particular in sociology, has well identified the significance of networks and networking behavior for a large set of important life outcomes, be it in job search, bargaining, or the marriage market.

Surprisingly, economists had long ignored the relevance of networks for economic behavior and outcomes – be it either implicitly, because it was simply not fashionable, or even explicitly, because it was believed that the deeper analysis of such topics could well be left to the “softer” disciplines in the social sciences. Only about 20 years after Granovetter’s seminal contribution, network research started to increase significantly in economics. The key questions – still, at that time mostly looked at from a purely theoretical perspective – were:

- How do networks form, i.e., what are the microeconomic equilibria that emerge from the interplay of individual incentives and social and economic interaction?
- and
- What are the implication of these network equilibria as well as of the dynamics of network formation on economic outcomes and welfare?

While the results of this research laid the groundwork for network analysis to become an accepted field in the economic literature, the ultimate proof that networks “really matter” (as I remember a colleague once saying) was still missing for a long time. For this, economic research had to go out and collect data, in particular, very detailed and sometimes complicated and messy data on how individual connections form, change, and adjust in important economic field contexts.

This is where Simon Heß' excellent paper that is awarded this year's Sturm & Drang Prize comes into play.

Together with his two co-authors Dany Jaimovich and Matthias Schündeln, Simon used the opportunity of a large field experiment by the World Bank in The Gambia to shed important light on the questions raised above. In particular, they analyze the effect of a large Community-Driven Development (CDD) program, in which a random selection of villages in The Gambia received a significant economic shock to their productive capital – in the order of more than US\$10,000 on average per village –, on the structure and strength of local economic networks.

It should be noted that informal networks very often play an even larger role in developing economies compared to industrialized countries due to the absence of formal (e.g., insurance) markets and that therefore, many international organizations and donors are increasingly targeting the inclusion of local communities in the design of their programs. It is thus of crucial importance to understand how such development programs affect a key dimension of local communities, namely social and economic networks.

Simon's paper documents two important and in my eyes intriguing findings. First, contrary to basic expectations the CDD program in The Gambia did not increase but actually *decreased* network interactions. The effect is sizable suggesting a loss of about one in six transactions per household on average. Second, the reason for this overall negative effect can be understood as the result of the interplay of three different channels:

- a) a potential increase in network interactions due to more joint activities as a consequence of the economic shock – this effect turns out to be basically zero in the data,
  - b) a potential decrease in network interactions due to a shift towards more market orientation – this effect is also only relatively modest,
- and finally,
- c) a potential decrease in network interactions as a consequence of an unequal distribution of the benefits from the economic shock due to favoritism and elite

capture in the village – this effect (unfortunately, one is tempted to say) turns out to be significant.

In sum, the paper thus shows that development interventions of the present type can have unintended consequences. It sounds a note of caution with respect to the ability and intention of these programs to foster community interaction. Obviously, CDD programs are not a panacea! While the overall welfare effects in the present context, e.g., in terms of a potential loss in informal insurance due to reduced network interactions, are found to be small, the paper nevertheless identifies and highlights an important mechanism CDD programs as well as future economic research are advised to take into account.

It is therefore with great pleasure that the selection committee has decided to award the Sturm & Drang Prize 2020 to Simon Heß for the best publication by a junior researcher in this year.

Frankfurt am Main

November 2020